OVERSIGHT OF THE OFFICE OF THE COMPTROLLER OF THE CURRENCY: EXAMINATION OF POLICIES, PROCEDURES AND RESOURCES

HEARING

BEFORE THE

COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED EIGHTH CONGRESS

SECOND SESSION

APRIL 1, 2004

Printed for the use of the Committee on Financial Services

Serial No. 108–78

U.S. GOVERNMENT PRINTING OFFICE

94–902 PDF WASHINGTON : 2004

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
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OVERSIGHT OF THE OFFICE OF THE COMPTROLLER OF THE CURRENCY: EXAMINATION OF POLICIES, PROCEDURES AND RESOURCES

Thursday, April 1, 2004

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The committee met, pursuant to call, at 10:18 a.m., in Room 2128, Rayburn House Office Building, Hon. Michael Oxley [chairman of the Committee] presiding.

Present: Representatives Oxley, Leach, Bachus, Kelly, Paul, Gillmor, Ose, Green, Feeney, Hensarling, Garrett, Murphy, Frank, Waters, Maloney, Gutierrez, Velazquez, Watt, Ackerman, Carson, Sherman, Lee, Inslee, Moore, Lucas of Kentucky, Crowley, Clay, Israel, Miller, Emanuel, Scott and Bell.

The CHAIRMAN. [Presiding.] The committee will come to order.

The committee meets today for the latest in a series of oversight hearings we have planned for this year on the Federal agencies under the Committee's jurisdiction. Last month, the Oversight and Investigations Subcommittee, under Mrs. Kelly's leadership, held a hearing on the operations of the Federal Deposit Insurance Corporation. Today, we turn our attention to the Office of the Comptroller of the Currency, the independent agency within the Treasury Department that charters, supervises and regulates the more than 2,000 institutions that make up the national banking system.

We are pleased to have back before the Committee the Honorable Jerry Hawke, who has recently returned from a brief medical leave to resume his duties as the Comptroller of the Currency. Comptroller Hawke, we welcome you back, and we wish you a continued speedy recovery, and from the looks of things, you are doing quite well.

In addition to reviewing the operations and regulatory policies of the OCC, today's hearing provides an opportunity to take stock of the health of the national banking system. Last week, the OCC released its report on the condition of national banks in the fourth quarter of last year, reflecting net income 21 percent higher than for the same period a year ago, markedly improved credit quality and record numbers for both return on equity and return on assets.

Even with all of the shocks that our economy has undergone over the past 4 years—beginning with the bursting of the tech bubble in 2000 and continuing through 9-11 and the scandals in corporate America—the fundamentals of the U.S. banking system appear to

have never been stronger. This surely bodes well for the sustainability of the economic recovery that has begun to take hold in recent quarters, as banks with sound balance sheets are well-positioned to make the kinds of loans to creditworthy borrowers that can help to fuel growth and create jobs.

One by-product of the record profitability that the banking industry has enjoyed in recent years has been an increase in merger activity among some of the country's largest institutions, including, within the past 6 months, three supervised by the OCC: Bank of America, Fleet and Bank One. While the trend toward consolidation in the financial services industry is not a new phenomenon by any means, these most recent mergers nevertheless raise important issues regarding the future structure of the banking industry.

As the primary Federal regulator for the Nation's largest and most complex banking organizations, the OCC faces a particular challenge in maintaining an examination force with the technical expertise necessary to ensure that these institutions are operated safely and soundly while continuing to meet the needs of the communities they serve.

Since its inception 140 years ago, the national banking system has offered banks that operate on a multi-state or nationwide basis the ability to do so under unified Federal supervision, and pursuant to one set of rules established at the national level. This fundamental principle, which has been reaffirmed in numerous Supreme Court opinions, has come under fire in recent months from opponents of regulations issued in final form by the OCC in February that seek to codify the supremacy of Federal law as applied to national banks.

As a State legislator for 9 years before coming to Congress, I do not dismiss lightly the claims by State banking commissioners and others that the OCC regulations undermine the dual chartering regime that has been a hallmark of the U.S. banking system since Civil War days. However, I simply cannot agree with my friends in the States that subjecting national banks to a patchwork of inconsistent standards set by State legislatures and local municipalities is either required by the dual banking system or in the best interests of the customers of those institutions.

In January of this year, Mrs. Kelly's subcommittee held the first congressional hearing on the OCC's preemption regulations. The hearing was a fair and balanced look at this complex issue, at which the OCC and its critics were both afforded opportunities to state and defend their positions. Since then, the OCC has taken several constructive steps to address legitimate concerns expressed by members and witnesses at that hearing. On March 1st, the OCC issued guidance to national banks stating the OCC's expectation that when national banks or their operating subsidiaries receive customer complaints forwarded by State authorities, they must take appropriate measures to resolve those complaints fairly and expeditiously.

Then last week, the OCC published a proposed rule that, once fully implemented, will result in a full listing of all national bank operating subsidiaries being available to the public over the Internet to facilitate the processing of consumer complaints against such entities. I applaud the OCC for taking these important steps, and

I encourage the agency to continue to reach out to its State counterparts to address areas of common concern.

Before I conclude my remarks, let me say a few words about Basel. This committee remains extremely concerned about the potential competitive impact that the Basel proposals might have on the U.S. banking system and about the continued lack of consensus among Federal banking regulators regarding the merits of the proposal. I will be particularly interested in hearing Comptroller Hawke's views on studies released recently by other Federal banking agencies addressing both the competitive issue and the potential effect of the new Basel framework on the prompt corrective action regime that applies to U.S. banks.

With that, I now recognize the gentleman from Massachusetts, Mr. Frank.

[The prepared statement of Hon. Michael G. Oxley can be found on page 52 in the appendix.]

Mr. FRANK. Mr. Chairman, I want to begin by expressing my full agreement with your last comment and indeed to thank the Comptroller for the work he is done with regard to the Basel agreement. We had our attention called to it, as you know, some time ago and confronted a situation which we thought was unbalanced and in which the full range of regulatory opinion wasn't being represented, and some legitimate concerns were not getting put forward. So I share your continued concerns about Basel, and I want to begin by saying in this case I think the Comptroller as well as the FJC have played a very useful role in giving us a chance to fully understand the implications of what was being proposed.

Now, no more Mr. Nice Guy. But I did welcome the chance to join you in that, because I want to make it very clear that what we are talking about here on the preemption issue are very profound differences of a policy and indeed even a philosophical nature. And they are not personal. I don't have any criticism; indeed, quite the contrary. I think the Comptroller has done an excellent job, and we are glad to see him back here in good health. But there are profound differences.

We had a hearing yesterday in this committee room in the Subcommittee on Capital Markets on proposals to basically reverse 60 years of American history in which insurance was essentially a State-regulated matter, and the degree of Federal takeover and Federal influence and Federal preemption was on the table. Today, we talk about an increase in power by the Federal Government over bank regulation, both in terms of the impact it has on national banks and in terms of the approach of the Comptroller's Office to try to increase the number of banks that are nationally chartered, partly induced by this particular set rules.

Last year, we passed, overwhelmingly, a set of rules which continued the preemption of the States on credit. Now, as we deal with these issue by issue, I think, Mr. Chairman, the time has come for us to begin to acknowledge what we are talking about. And the question is this: To what extent are the States at all economically relevant? An argument can be made that they are very diminished relevance.

And we talk about globalization and obviously nationalization is a small piece of globalization. The greater includes the less here.

But what we have got—this is not a matter of making partisan points about who is for States' rights or not—there does appear to be a significant shift in opinion, certainly on the majority side, shared to some extent on our side in various centers of opinion, that the time has come significantly to diminish the role of the States in economic regulation. Now, that is something we shouldn't just be dealing with piece by piece; we have to confront it.

Part of the problem is, and this is where it gets trickier in particular, the States have traditionally taken a lead role in the consumer protection area. And I forgot to add as I talk about this concern about the diminishing role of the States, we had a prolonged debate in this committee about whether or not we should increase the role of the Federal Securities and Exchange Commission and diminish the role of State regulators in the securities area. We ultimately resolved that, Mr. Chairman. I thought you played a very useful role in that. We resolved it, but I think it is a very reasonable way by directing the SEC and urging the States to talk about coordination.

But there is a pattern here: Securities regulation, insurance, the granting of credit. Now, we are talking about national banks, particularly predatory lending and other consumer roles. In every case, we are talking about a significant shift from State to Federal power, and it ought not to be done piece by piece; we need to really look at it. This committee is best positioned to do that.

Now as to the specifics here. I really want to urge my friends in the banking community to reconsider the notion that the way to deal with this complex set of issues is by regulatory action alone. This is not a technical matter, and it is not a matter of whether or not the law allows it. That is to be ordered in court, and we are not a court. We decide what the law should be, not what the law is. The implications of this are far-reaching. The Comptroller has said, "Well, this is just the way the law always was." I must say that I am unpersuaded that every Attorney General and every bank commissioner misunderstood the law previously, because it is the unanimous opinion of every Attorney General and every bank commissioner that this represents change. Change isn't necessarily bad, but I don't think it serves us in dealing with important philosophical and economic and policy issue to act as if it really isn't an issue at all.

And I want to say to my friends in the banking community, I understand that you would like to deal with this. To some extent I must say I get a little bit of the Thomas a' Beckett emanation from my friends in the financial community, "Will nobody rid me of this meddlesome priest?" The meddlesome priest being the States, and they swat him over here in credit and swat him in insurance. Well, be careful, that didn't work out so well for King Henry. Don't get yourself—is that the right king? Don't get yourselves in the same kind of position. I will ask to revise and extend if I got the king wrong.

And I would just ask for one more minute, Mr. Chairman, if I might, just to say because this is such a thoroughly important issue, let's use a different model. Last year, many of the people in this room, both on our side and in the audience, consumers and members of the industry and regulators collaborated on a bill

which extended Federal preemption in the extension of credit in a way that reached pretty good consensus. Our friends from California were understandably concerned because California had been in advance here and to my regret we weren't able to protect California's decision as much as I would like, but for virtually everybody else in the country we preserved the function that credit plays in the economic system while increasing for literally everybody outside of California the degree of consumer protection and giving a reasonable amount of consumer protection.

I urge my friends, let's work together to duplicate that process. Do not think it is a good idea simply to use the fact that you have got the existing legal authority and push through something that is so controversial. It is not good for the stability of the economic system. One of the things we want is a sense that what we have done will go forward.

When every Attorney General and every bank commissioner, Republican and Democratic, is so stridently in opposition, when you have a very strong bipartisan leadership of the chairwoman of the Oversight Committee, the gentle woman from New York, ranking member, the gentleman from Illinois, working together this is not the way to do it. Yes, there are arguments for preemption, there are arguments for economic uniformity, there are concerns about whether that is done with adequate consumer protection. Clearly, the Comptroller does not have statutorily the ability to deal with predatory lending that most of the States think or many of the States think are necessary.

So I ask the people, let's join together and in the case of the question of the authority of the Comptroller to preempt and deal with national banks, let's follow the model that we followed last year. It is my impression that my friends think that ended well, and even some people who may not be such great friends, but all of us together, I think, thought we had a pretty good process. We preserved the economic needs of the system, and we provided consumer protection and you have a stable consensus system that will go forward. It is not in the interest of the financial community longer term, no matter what you think short term, to use your muscle to push something through that is inherently unstable because of the degree of resistance it has.

And I would just close by saying, Mr. Chairman, I think we demonstrated on both sides of the aisle last year our ability to come together and deal with these issues in a sensible, balanced way. Please, let's follow that model again.

The CHAIRMAN. The gentleman's time has expired. Under the rules of the Committee, the Chair is prepared to recognize members for three minutes for opening statements.

With that, I recognize the gentleman from Iowa, Mr. Leach.

Mr. LEACH. Just briefly, I would like to comment on the parameters of what was just discussed but from another issue perspective, and that is the contrasting role of States and the Federal Government. This committee has recently passed a significant banking reform legislation that ironically moves in a little different direction than the ranking member just indicated; that is, we are empowering five States to give authorities that have never existed before in the American financial services community, and that is to

give the effective power, full power of banking to a charter called the ILC charter. And this takes out of the loop the preeminent Federal regulators of holding companies, that is the Federal Reserve, and puts what in effect is an uneven playing field in regulation in the system all at the command of the potential of five States.

And I would only raise this in a significant way in terms of competitive inequity but also in breaches of the current framework of banking where holding company regulation has always been something that we have considered of significant dimension but also in terms of the breaching of commerce and banking where, quite literally, Congress is contemplating giving powers to non-banks greater than powers that are given to banks. And this is a very significant issue that I think ought to be seriously reviewed, and it is an aspect of decentralization that I consider to be wholly unhealthy. It has one modest effect of devaluating all bank charters in America.

And as the comment was made to friends in the associations, I would say, quite frankly, that several of the associations representing America's commercial banks have let down their community very significantly and that people ought to be thinking about this quite seriously from the perspective of the manner in which American economy is organized, the notion that some large institutions can breach the commerce and banking parameters in ways that have never been breached in modern day before is also very significant circumstance.

And so it is my view that we have to be very careful as we weigh these issues of States' powers versus Federal powers and recognize that while there can be competitive pluses and minuses, there also can be a real social change that can occur if we are not very careful.

Thank you, Mr. Chairman.

The CHAIRMAN. I Thank the gentleman.

The chair now recognizes the gentleman from Illinois, Mr. Gutierrez.

Mr. GUTIERREZ. Thank you, Mr. Chairman. Good morning. I want to thank Sue Kelly, my Oversight Subcommittee chairwoman for originally calling this hearing to follow-up on our hearing of January 28. I am pleased that Comptroller Hawke has recovered sufficiently from his illness to join us here today and wish him again a speedy and full recovery.

Due to the great interest in this issue, now it has become a full committee hearing, so I am happy to see that it has been expanded, the interest in this very, very important issue.

I would also like to thank Ms. Kelly and Mr. Paul for their work on this important issue of OCC preemption. We are committed to working together with a number of our other colleagues on both sides of the aisle, including Ranking Member Frank, to ensure that our States have the power to protect consumers and to stop the OCC from eroding strong safeguards that have been used by States for more than a century to enforce consumer protection laws.

It seems to me to make no sense for the OCC to attempt what many consider an unprecedented and unchecked expansion of its authority when States currently have the tools and the resources

to effectively enforce consumer protection and other important laws.

As many of you know, since our last hearing in January, representative Ron Paul and I passed an amendment to the Financial Services Committee's budget views expressing concern regarding budgetary effects of the OCC's recently published preemption rules. The budget views now put the Financial Services Committee on record that the OCC's preemption rules represent an unprecedented expansion of authority and one that was instituted without congressional authorization.

Let me just ask that the rest of my statement be included for the record, and with no objection, Mr. Chairman, I would just like to end with a few brief comments.

The CHAIRMAN. Without objection.

Mr. GUTIERREZ. Thank you, Mr. Chairman. I would like to see, Mr. Hawke, if we could follow up and expand on what I know your conversations with me and other members of this committee and the House as you recover from your illness to talk to us about this issue. And I want to thank you for taking the time to come to my office, sitting down and speaking with me.

I think we have a difference of opinion, and I think people can hold differences of opinion, but I think at the same time what we are looking for, what you are looking for, I know what I am looking for and other members of this committee is that consumers be protected and that the soundness of our banking system be protected in this nation. Both of them are important and shouldn't have to compete with one another.

I think that if we brought bank examiners together, if we brought Attorney Generals together from throughout the States, if we brought your office and the good offices of this committee and others and sat down at a table where we could—not in some back room but quietly sit down in an open discussion so that we can share frankly our views and find that road that allows us to protect our consumers, which is our primary goal in this issue, and you to fulfill your responsibilities to the soundness of our banking system as one of your main goals, and also I agree with you, consumer protection, I think we can all reach that together. So I hope that after this hearing we can continue to do.

We are going to take an additional step, Mr. Chairman, and that is that Congresswoman Sue Kelly and I are sending today this letter to the Honorable David Walker, Comptroller General of the General Accounting Office. We will give Mr. Hawke a copy of the letter where we ask for them to see whether or not these are unprecedented moves and whether or not statutorily they can do what they say along with other consumer protection issues.

Thank you so much, Mr. Chairman.

[The prepared statement of Hon. Luis V. Gutierrez can be found on page 55 in the appendix.]

The CHAIRMAN. The gentleman's time has expired. Are there further opening statements? If none, we will now turn to the gentleman from New York seeks recognition for an opening statement?

Mr. ISRAEL. Yes, Mr. Chairman.

The CHAIRMAN. You are recognized for three minutes.

Mr. ISRAEL. Thank you. I want to thank you, Mr. Chairman and the Ranking Member Frank for conducting this important hearing today on OCC and their recent regulations. I also want to thank my colleague from New York, Ms. Kelly, as well as my good friend, Mr. Gutierrez, for leading the charge on this important issue. While I am not in agreement entirely with their stance, I am pleased that this important debate is taking place.

I also want to thank our witness, Comptroller Hawke, for being here today.

The discussion of late concerning the OCC has been about the issue of preemption and the powers of the OCC. But I believe the issue is bigger than that of the powers of national versus State-chartered banks or the presumed powers of the OCC. The real question here deals with ensuring the greatest protection of all American consumers with respect to stopping abusive lending practices.

While I welcome the approach undertaken by the OCC of creating one uniform Federal standard for all national banks and their operating subsidiaries with respect to predatory lending as a way of creating a level playing field for all national banking customers, I also believe the regulations they have put in place on this front are weak at best. Our constituents have no idea where their bank is chartered, and, quite frankly, they don't care. But they do care about protecting their money and their investments and keeping the access to capital free-flowing.

The establishment of this national albeit weak standard by OCC drives home the need for real action by Congress this year to address predatory lending with a strong national law that governs lending at all financial institutions and their operating subsidiaries, regardless of where they are chartered.

These are the issues we need to address in Congress. Thankfully, these actions by the OCC have had the desired effect of reigniting the discussion about real legislation to address the issue of non-prime lending and our Nation's diverse patchwork of regulations governing it. Congress needs to develop legislation to create a new uniform Federal standard in lending practices that crushes predatory lending by correcting the non-prime market which continues to furnish capital to neighborhoods that were traditionally denied these resources, and I represent many of those types of neighborhoods.

I look forward to today's hearing and hope for a good back and forth volley on questions and answers, not only on the issue of OCC regulation but, more importantly, on the larger issue of the need for congressional action to address lending abuses this year to protect all banking customers regardless of where their bank is chartered.

And I thank the chair and ranking member again for allowing me this time to speak, and I yield back the balance of my time.

[The prepared statement of Hon. Steve Israel can be found on page 57 in the appendix.]

The CHAIRMAN. The gentleman yields back.

The gentleman from California, Mr. Sherman?

Mr. SHERMAN. Thank you. This seizure of power by the OCC is sweeping away congressional intent, sweeping away all State laws.

It is illegal, it is wrong and it is politically stupid. It is illegal because you can't go way beyond anything Congress ever intended in terms of changing the way that our whole financial services industry is regulated. It is wrong because you have exposed consumers in my State to practices that my legislature wishes to prohibit without legislative hearings in this Congress. It is wrong because you have given a competitive advantage to one group of financial institutions over another, and, coincidentally, they happen to be the biggest, the most powerful and the biggest campaign contributors in the financial services industry.

And it is politically stupid because neither the administration nor the majority party can disclaim responsibility for the harm to our Constitution, to our Federalism and to consumers that this is going to cause. Your agency does not have the capacity to deal with the consumer complaints, so you are really saying the consumers will have no way to complain. Your agency does not impose the limits on predatory lending that even this committee would feel necessary as part of national standards. The majority party cannot escape responsibility for this attach on Federalism and attach on consumers and attack on smaller businesses trying to do business with the national banks. You are part of the administration which must bear responsibility for your decisions.

The majority party could put an end to this by a suspension bill this afternoon but has not done so. Instead we will await the action of the American people this November as they see that this fits into a pattern of unbridled corporate power and the unleashing of this corporate power, whether it is arsenic in our water or predatory lending in our real estate transactions.

The CHAIRMAN. The gentleman yields back. Is there further—the gentleman from Georgia, Mr. Scott?

Mr. SCOTT. Thank you very much, Mr. Chairman. I appreciate this opportunity. Mr. Hawke, thank you very much for coming.

I am from Georgia, served in the Georgia legislature for over 25 years, worked in banks and banking committee for all of those 25 years. As you know, we are in the catbird seat, one of the leading players in our fight against predatory lending. When you preempted Georgia's fair lending law, there were many concerns that were raised. One, that it might dilute consumer protections, it would be harmful to our dual banking system.

But the most significant concern to me is this one: That the OCC and you, perhaps, Mr. Commissioner, and your failure to respond to a letter which was written by my commissioner, David Sorrell with the Georgia Department of Banking and Finance. And that letter was dated August 21, 2003. Seven months, Mr. Hawke. That is very, very disrespectful—disrespectful to Georgia, disrespectful to the people of this country that the OCC would preempt a State law.

Our folks in Georgia in the catbird seat, one of those affected the most, we write letters and not one response in 7 months. And this letter regarded three issues concerning the OCC's preemption of the Georgia's Fair Lending Act.

And Mr. Chairman, I would like to in the interest of time submit this letter for the record, if I may.

[The following information can be found on page 91 in the appendix.]

The CHAIRMAN. Without objection.

Mr. SCOTT. I would also like to submit a letter on March the 9th, 2004. Again, our banking commissioner of Georgia, Commissioner Sorrell, again wrote the OCC; no response. And he sent copies to our entire congressional delegation.

Again, Mr. Chairman, if I may, I would also like to submit this March 9 letter for the record——

The CHAIRMAN. Without objection.

[The following information can be found on page 93 in the appendix.]

Mr. SCOTT.——if I may.

The CHAIRMAN. Without objection.

Mr. SCOTT. Which includes, Mr. Chairman, which includes a detailed chronology of the efforts that our State of Georgia has taken to solicit a response from the OCC. Very disrespectful and disregard, Mr. Hawke. I am not convinced yet that we do need a national law to regulate predatory lending practices or what standards would be written into such a law. That very well would preempt the States. My mind is open on that issue. However, the OCC's actions are a good reason for Congress to assert some authority on these issues.

And while the Georgia Fair Lending Act was indeed a flawed law concerning the assigning liability, we were responding to a very serious issue of predatory lending in that State. Georgia is the poster child for abuses of predatory lending. Federal regulatory preemption should be conducted in an open manner with adequate opportunities for comment and surely secure the respect of the OCC.

The CHAIRMAN. the gentleman's time has expired.

The chair would indicate to Mr. Hawke that the reason that the chair decided to have this hearing in the full committee was, as you can tell, there are a lot of strong opinions about the issue, and I thought it would be helpful to have a full committee hearing in that regard as opposed to the Oversight Subcommittee. And I think from the tenor of the debate, I think you can tell that this is why I made the decision I did.

Again, we welcome you back to the Committee and you may begin.

STATEMENT OF HON. JOHN D. HAWKE, JR., COMPTROLLER OF THE CURRENCY

Mr. HAWKE. Thank you, Mr. Chairman, Ranking Member Frank and members of the Committee. I welcome the opportunity to appear before the Committee to review both the condition of the national banking system and the Office of the Comptroller of the Currency and to address other issues of particular significance. I think that members of the Committee have raised some very significant issues this morning that are very much worth discussing in greater detail.

I also should say, Mr. Chairman, that I very much appreciate, on a personal level, the statements of good wishes with respect to my return to work, and I can only say that I hope I feel as good after this hearing is over as I did coming into it.

The national banking system, approximately 2,100 financial institutions, holding 56 percent of all commercial banking assets, is in excellent health. By historical standards, the system is exceedingly well-capitalized. Today, all national banks, with minor exceptions, have risk-based capital above 8 percent, and less than 1 percent of national banks have risk-based capital below 10 percent. In 2003, the national banking system set new earnings records as measured by return on equity and return on assets.

National banks continue to play their traditional role as a key source of investment capital to America's businesses and communities. In 2002 and 2003, total bank loans grew by 7.8 percent and 7.6 percent, respectively. Consumer loans and loans backed by commercial and residential real estate have seen particular growth. Consumers have tended to use funds from mortgage refinancing and home equity lines to pay off higher interest credit cards and installment debt, a trend that has helped sustain overall consumer spending and that has been widely credited with having eased the duration and severity of the 2001 recession.

Credit quality today is also strong, particularly for this stage of the economic cycle. The OCC continues to monitor developments in areas that present vulnerabilities, such as small business lending and certain real estate markets and property types.

Let me now turn briefly to the condition of the OCC, an organization of some 2,800 people—1,700 of them bank examiners in the field. Their skill and professionalism are recognized and respected—and, in my view, unmatched—around the world. Our people work out of the OCC's Washington headquarters, the Ombudsman's office in Houston, and our 4 district offices, 49 field offices, and 23 satellite locations in cities throughout the United States, and our examining office in London. In our large bank program, we have teams of full-time examiners on-site, as many as 35 or 40 in our 25 or so very largest banks, and they constantly monitor the condition of those banks.

The OCC receives no appropriated funds. All of our funding is derived from assessments and fees received from national banks. We have focused on modernizing our financial operating systems and ensuring that we manage our financial resources wisely. The agency's budget has been balanced every year during my tenure as Comptroller, and we have been building our strategic contingency reserve to ease the impact of unforeseen disruptions to our operations or unexpected demands on our resources. Our present goal is to build the reserve to equal 6 months' operating expenses, a goal that we expect to achieve in mid-2005.

The OCC's financial condition and the strength of its resources have taken on wider significance in light of some of the questions that have been raised about whether the OCC has sufficient resources to assure adequate protection for customers of national banks and their subsidiaries. These questions have been raised, as they have this morning, in the context of our recent regulations relating to the applicability of State laws to national banks and the role of State officials in enforcing consumer protection laws against national banks and their subsidiaries.

I would be pleased to discuss these regulations in further detail, but let me state emphatically that neither regulation involves any

fundamental shift in regulatory roles or responsibilities, neither alters the OCC's continuing commitment to consumer protection, and neither should impose new or unmanageable burdens on our enforcement and compliance resources.

We are proud of our long record of protecting consumers against abusive and unfair banking practices and developing supervisory innovations that have advanced that goal—innovations that have been emulated by other financial regulatory agencies. We have pioneered the use of section 5 of the Federal Trade Commission Act as a basis to take administrative enforcement actions against unfair and deceptive practices; we have thwarted payday lenders and their strategy to evade State laws through alliances with national banks; we have secured millions of dollars in direct restitution for consumers; we have developed comprehensive supervisory guidance to warn banks of the consequences of engaging in predatory lending; we have adopted special procedures to assure full and prompt consideration of customer complaints referred to us by State officials and much more.

Indeed, our new preemption rule materially strengthens our ability to fight predatory lending by prohibiting national banks from making any consumer loan based predominantly on the foreclosure or liquidation value of a borrower's collateral and disregarding the crucial question of whether the borrower can afford the loan. I think this issue lies at the very heart of predatory lending. Our advisories on predatory lending caution banks that if we find evidence of abusive practices, we will not only take strong enforcement action but we will take it into account in evaluating the institution's CRA performance.

At the OCC, consumer protection is a long-standing and integral part of our mission. Over 100 OCC examiners throughout the country are compliance specialists. They not only perform detailed compliance examinations but also serve as expert advisors on consumer protection issues to other examiners. And our 1,700 person strong field examination staff is backed by dozens of attorneys who work in enforcement and compliance.

I would point out by way of comparison that State banking departments collectively supervise about 113,000 entities, of which approximately 6,000 are commercial banks. For all of these entities, the Conference of State Bank Supervisors reports that the States have a total of 2,308 examiners at their command. In other words, if each and every State examiner spent 100 percent of their official time examining commercial banks, leaving all 107,000 savings banks, thrifts, credit unions, mortgage bankers, payday lenders, check cashers, pawn shops and other sundry financial providers that variously fall under State authority entirely unsupervised, the OCC's supervisory resources would still outstrip those of the States. The chart attached at the end of my written statement illustrates this comparison.

Supplementing the work of our examining corps is our Customer Assistance Group, or CAG, which is co-located with the OCC's Ombudsman's Office in Houston. In 2003, this world-class operation processed more than 70,000 complaints and inquiries from bank customers in a prompt and sympathetic manner. It has also served as a de facto clearinghouse of complaints and inquiries that have

been addressed to us but which really belong in other agencies. We have distributed to the Committee this morning a chart that shows the extent of the referrals that our Customer Assistance Group effects every year. Last year we received 6,550 referrals from State agencies, and we referred over 13,000 inquiries and complaints to other Federal and State agencies, including 755 primarily to State banking agencies.

While some have mistakenly concluded that CAG is the means by which we carry out our enforcement and compliance responsibilities, that is not at all the case. Enforcement and compliance remains first and foremost the responsibility of our large battery of examiners and attorneys. The CAG is a very important adjunct to that resource. For example, we carefully track the volume of complaints we get, bank by bank, and if we see troubling patterns develop, CAG will promptly get our examiners involved to look into what might be going on at the bank to cause such a result. And we have had very good results from that.

The OCC also cooperates with State authorities to accept referrals when the States receive a complaint regarding a national bank, and we make referrals to State authorities when we get a customer complaint regarding a state-supervised institution, as the data that I just referred to demonstrates. I think it is obvious from that data that the OCC and the States are already working together on a routine basis to help bank customers resolve their issues, and we would like to build on that foundation.

We have invited State bank supervisors and State attorneys general to visit our Houston office to learn more about how we handle consumer complaints. We have established special procedures to handle and track referrals from State authorities concerning national banks and their subsidiaries that are alleged to have engaged in abusive or predatory practices. We issued a new advisory letter to national banks clarifying our expectations about how they should handle consumer complaints forwarded to them by State agencies, and we have made it clear that we will not look kindly on a bank that cites the OCC's exclusive visitorial power as a justification for not addressing referred complaints or providing information about the disposition of complaints to State agencies. And we have proposed a model Memorandum of Understanding to facilitate the sharing of information about consumer complaints with the intent of providing effective coordination of enforcement activities with State agencies.

By coordinating resources and working cooperatively with the States, we are convinced that we can maximize benefits to consumers, close gaps between existing consumer protection laws, and most effectively target financial predators. And we welcome further dialogue with the States to explore those goals.

One recent example is the coordination related to Security Trust Company, which was involved in the mutual fund scandals in Arizona. We worked with the SEC and with the Attorney General of New York very effectively and with great good will in that case.

Finally, let me say a few words about the Basel II process. This is an enormously complex and important project, and the OCC has been deeply involved in it for more than 5 years. There are still important issues to be resolved as we approach the Basel Committee's

target date of mid-year 2004 for the release of a "final" paper, and we will continue to work hard on those issues.

The important thing to understand about this process is that it is far from over. Before we adopt final implementing regulations for national banks, there are a number of important domestic processes that need to be completed. First, we must complete a new quantitative impact study, as we promised this committee, so that we will have a much sounder basis for estimating the actual impact of Basel II on the capital of our banks. Second, we must complete the economic impact analysis required by Executive Order 12866 so that there will be a much clearer understanding of the implications of Basel II for our economy. Third, we need to continue the dialogue with this committee and its counterpart in the Senate on the progress of this process and the issues that have been raised. Finally, we must draft and then put out for comment our final implementing regulations.

I am confident as this process moves ahead we will uncover a great many more issues that will require us to go back to the Basel Committee for appropriate responses. I also feel confident that the current implementation date of year-end 2006 will be difficult, if not impossible, to realize.

Let me say, Mr. Chairman, that the interest and involvement of this committee in this very difficult process has been of enormous value to us. Other members of the Basel Committee have followed very closely the proceedings of this committee and the public statements of its members on Basel II. This has not only strengthened our hand in the negotiation process but has sent the message that all legislators intend to have an important role in the oversight of this process, and for this we are very grateful.

In conclusion, Mr. Chairman, the national banking system is sound, and its recent performance has been strong. It has successfully weathered the recent recession, and it is responding in dynamic fashion to changes in the financial services marketplace. The OCC, too, is keenly focused on keeping pace with change. We look forward to working productively with you, with members of this committee and with State officials as we pursue our efforts to achieve that goal.

Mr. Chairman, I wondered if I could just take one additional moment on another matter. I want to pay tribute here to those employees of OCC who have been called to active duty in Iraq and particularly to four members of our staff who volunteered to go to Iraq as part of the U.S. team that is helping to rebuild that country. These courageous OCC staffers are working on the rehabilitation of the Iraqi banking system and are doing a fantastic job. They are in harm's way every day, but they are demonstrating real dedication and we are enormously proud of all of our OCC colleagues that are serving in Iraq.

Thank you, Mr. Chairman.

[The prepared statement of Hon. John D. Hawke Jr. can be found on page 60 in the appendix.]

The CHAIRMAN. Thank you, Mr. Hawke, and we all share your pride in the OCC folks who are in Iraq, particularly after recent developments in Iraq. They are very brave and strong Americans, and we appreciate their service.

You mentioned Basel II at the end of your comments. It was about a year ago or so when you testified here before the Committee regarding both your substantive and procedural concerns about the Basel II capital proposal. What is your current position regarding the Basel II? I know we look forward to the quantitative impact study, which will be an integral part of the decision-making process. When can we expect that, and, just generally, where are we? In fact you indicated the 2006 goal would be difficult to attain. If you could give us a little better feeling for that date as well.

Mr. HAWKE. I would be happy to, Mr. Chairman. The Basel Committee is meeting in May, and it is expected that a as a result of the May meeting what I refer to in quotations as the "final Basel paper" will be put out. It is not final except to the extent that it allows domestic processes to move ahead with something that has more specifics than we have seen in the past.

There are still some very important open issues we are discussing here in the United States, for example, on an interagency basis, the treatment of retail credit and particularly credit cards. I have felt very strongly that we must be very careful not to adopt rules that have unintended adverse consequences for the enormously successful consumer credit industry that our banks have helped to develop in this country.

After the Basel Committee comes out with its mid-year paper, we will begin the conduct of the quantitative impact study, which I think is enormously important because we don't really have a solid basis today for determining—estimating the impact of Basel II on the capital of our banks. Following the quantitative impact study, we will begin to prepare domestic rulemaking matters that will translate Basel II into domestic rules, and we will continue the dialogue with this committee.

During that process, I expect, based on past experience, that numerous issues will be raised that will cause us to go back to the Basel Committee for change or clarification. Just the quantitative impact study, for example, might tell us that the results of Basel II are that there will be an unacceptably expensive impact on the capital of our banks. We need to know that before we sign on to anything. So there is a lot of process still to come and an important role for the dialogue between us and the Basel Committee.

The CHAIRMAN. Thank you. You have talked about your willingness to talk with State officials regarding ways to improve the handling of customer complaints, and I understand you have an agreement with State insurance regulators in all of the 50 States. Can that serve as a model for working with the State banking supervisors as well?

Mr. HAWKE. I think it could be a very compelling model. We were not always together with the State insurance commissioners on substantive powers issues, but we have been able to put those issues aside. Congress resolved most of them in Gramm-Leach-Bliley. We now have agreements with 48 State insurance commissioners, and those agreements provide a very effective mechanism for the exchange of information and the referral of complaints about practices engaged in by the insurance affiliates of national banks. We also meet regularly with the National Association of Insurance Commissioners.

The CHAIRMAN. The concern has been expressed in some quarters that the OCC's regulations clarifying the applicability of State laws to national banks and their operating subsidiaries would somehow authorize those entities to engage in real estate brokerage activities. My reading of the regulations and current Federal law, namely Gramm-Leach-Bliley, suggests that there is no basis for this concern. Is that an accurate assessment?

Mr. HAWKE. That is completely accurate. It is unfortunate that the realtors have persisted in misreading our rules, and we have tried to counsel with them and explain that nothing in our regulations remotely bears on real estate brokerage. National banks are not permitted to engage in real estate brokerage even though banks in 25 or 30 States are permitted to do that. This is an issue that is vastly premature. It relates to the realtors' fight with the Treasury Department and the Fed over rulemaking under Gramm-Leach-Bliley. It has nothing to do with national banks or the OCC's recent regulations.

The CHAIRMAN. Thank you for clearing that up. Finally, in the past year, we have seen several major mergers involving national banks and the creation of an increasing number of megabanks that operate globally. What challenges does the rapid pace of industry consolidation pose to the OCC as the primary Federal regulator for Federally chartered banks? In that vein, we can all recall for a number of years when the largest banks in the world were listed, there would be maybe one U.S. bank in that category and several Japanese banks.

The world has changed dramatically. There was a lot of concern expressed in a lot of quarters that where were the American banks in this new global economy? And it appears now we are very competitive in that area and will continue to be so, but what kind of pressures and goals does that present to you?

Mr. HAWKE. Well, let me say first, Mr. Chairman, that we already supervise what I think could fairly be called megabanks. We have several banks in our portfolio that are extremely large, approaching, if not exceeding, the trillion dollar mark. And so we have had a fair amount of experience on the supervisory side in dealing with them.

The expansion of the number of megabanks and the growth of the existing large banks will certainly present challenges. There will be an added degree of complexity. The risk management systems, the modeling that they use will become more complex, and we have got to keep up with that. The kinds of instruments that they issue will become more sophisticated. We have excellent people working in all those areas, and I think we are quite ready to take that challenge on. But we are spending a good deal of time in reviewing just how we supervise these large banks.

As I said before, at the very largest banks, we have full-time, onsite teams of examiners. So our mode of review in these banks is continuous supervision. We are intimately involved with them all the time, and we will continue to be.

The CHAIRMAN. Thank you.

The gentleman from Massachusetts.

Mr. FRANK. Thank you, Mr. Chairman, and I want to join you in expressing our support for the words that Mr. Hawke mentioned

about the people serving in Iraq. That is a very important contribution.

I want to call people's attention to the CD that we are about to show that preaches Mr. Hawke. You are about to see Mr. Hawke in stereo.

Mr. HAWKE. Before he lost weight.

Mr. FRANK. You can use this as before and after.

(VIDEO)

Mr. HAWKE. "I am Jerry Hawke, the 28th Comptroller of the Currency. Banks in the United States have a unique privilege: The right to choose their primary regulator. The Office of the Comptroller of the Currency is the primary regulator of banks that hold the national charter, a unique and powerful instrument for carrying on the business of banking. How the OCC and the national charter can help banking organizations achieve their goals is the subject of this presentation."

Mr. FRANK. Thank you, Mr. Chairman. That is a teaser, and if people want to see the whole thing, I am a great respecter of intellectual property, they can contact—I don't know, Jerry, you can give your web site later on and maybe they will download it without paying for it and we will get——

Mr. HAWKE. We have got extra copies.

Mr. FRANK. Yes. I appreciate that you do. We are not in a static situation, we are in a dynamic situation, and part of the concern we have, many of us, is as made clear here. The emphasis on the preemption, the firmness of this, the great scope of it, OCC says, "Well, it has always been that way." People didn't know it was always that way, and, clearly, the intention of that is to persuade people who have State charters to come to Federal charters. The problem I have is that it is not purely what we think of as banking activities. You have operating subsidiaries.

With regard, for instance, to predatory lending, you have made the point that there hasn't been a great deal of accusations in predatory lending at national banks to date accurately. But, again, you are out there advertising, you are encouraging people to come to be regulated by you under these new rules and change their charters and with this preemption. That is part of the problem.

In particular, I was troubled in this article that is in the Wall Street Journal for the 28th of January by Jess Bravin and Paul Beckett called, "Friendly Watchdog." I would ask unanimous consent it be put in the record.

The CHAIRMAN. Without objection.

[The following information can be found on page 87 in the appendix.]

Mr. FRANK. Here's the example that is particularly troubling to me. In Michigan, the State Motor Vehicle Sales Finance Act passed in 1950 requires auto dealers fully disclose installment payment terms, limits document preparation fees and restricts the conditions under which a car can be repossessed. The statute applies only to dealers who sell cars through installment plans.

You have now preempted that, because the National City Bank, which is part of the National City Corp and the Huntington National Bank owned by Huntington Bank Shares of Columbus, Ohio has this relationship with the dealers who market their car loans.

As a result of your preemption, Michigan's law which applies to car dealers now doesn't apply to car dealers if they are affiliated with a national bank.

What is so important to the uniformity of the banking system that you now have to bifurcate Michigan's administration of its laws applying to car dealer loans? Because if you buy a car on the installment plan and it is financed, I guess, by GMAC or by a State bank, it is one thing, but if it is by a national bank, those laws don't apply. Then, additionally, what laws have you got, what rules do you apply? Are there comparable rules that you apply to protect people who buy cars under the installment plan?

Mr. HAWKE. Well, let me say first, Mr. Frank, that preemption of course is a constitutional doctrine, and we——

Mr. FRANK. Mr. Hawke, that is not what I asked you. I have only got a limited amount of time. What rules have you got to protect car buyers?

Mr. HAWKE. We don't have any rules that——

Mr. FRANK. Any rules at all. So the effect in Michigan was that you canceled out those Michigan rules passed in 1950 and continued—apparently, Michigan hasn't felt any need to change them in, what, 65 years? And you substitute nothing. Is that a good system? I mean now that you have made this clear, do you plan to adopt some rules dealing with people who buy cars?

Mr. HAWKE. We don't have any such intentions. But, Mr. Frank, I think it is important to recognize that that law prevented national banks effectively from making loans through car dealers, and it was a direct interference with the exercise of their Federal powers.

Mr. FRANK. How did it prevent them? Did it prevent anybody else from making loans through car dealers? Are there no loans through—I mean what about State banks, do they make loans through car dealers?

Mr. HAWKE. I don't know what State banks do.

Mr. FRANK. Well, they probably do. I mean you say it prevented them. It prevented them from making loans totally unrestricted, but of all places I think Michigan is probably a State where buying cars probably didn't get interfered with. I mean they like buying cars and selling cars in Michigan. So the notion that the State of Michigan would for 65 years have maintained on its—it is 55 years, my arithmetic's off—the notion that for 55 years would have retained on it books a law that made it hard for banks to finance cars is not credible. This is an example.

Let me, and we are running out of time, so I just want to say why are you sending out the video? I mean do you have an institution or interest in getting banks to switch? Why do you care? I mean shouldn't it just be that you are out there and if banks want to be national, you do this, and if they want to be—why are you recruiting? Why are you out there trying to encourage them to change their charter?

Mr. HAWKE. Well, I will be happy to address the question why we prepared that video, which was done for——

Mr. FRANK. No, that is not what I—why are you out there trying to get them to change?

Mr. HAWKE. I would like to answer the question that you raised about why we distributed the video, Mr. Frank, if I may. The reason that we prepared that video was because we get hundreds of questions all the time from organizers of banks, from lawyers and consultants who want to put banks together, and they ask us what can we tell them about the charter choice that they have to make.

Mr. FRANK. Who did you send the video to, Mr. Hawke?

Mr. HAWKE. If I can finish my answer, Mr. Frank.

Mr. FRANK. No, because you are going to filibuster. I agree with you on some things, but I don't want this—I am asking you very specific questions, and I think you are frankly evading the point. I think you sent that video in substantial part to persuade State-chartered banks to switch their charter.

Mr. HAWKE. We send that video to people who are interested in knowing what the difference is between a national charter and a——

Mr. FRANK. That includes State-chartered banks, right? Do you only send it out to people who ask you or did you—I mean is this like a—is there a "don't video me" list?

Mr. HAWKE. No. We make it available to——

Mr. FRANK. Did you send this unsolicited to a lot of State banks?

Mr. HAWKE. We don't send it out unsolicited. We make it available to anybody who wants to pick it up at——

Mr. FRANK. What do you mean make it available?

Mr. HAWKE. Mr. Frank, what we did——

Mr. FRANK. What do you mean by make it available?

Mr. HAWKE. We have it available when bankers' groups come through to visit us. We make it available——

Mr. FRANK. Do you suggest—do they ask you, "Hey, I heard you have got this hot new video, the Jerry Hawke video." How do they know about it, these State banks?

Mr. HAWKE. I will tell you what happens. The State bank supervisors are out there very aggressively marketing——

Mr. FRANK. No, no. Come on. I am sorry, now, Jerry, you are just filibustering. What do you do to make it available to State banks? Do you take the initiative in sending that video to State banks?

Mr. HAWKE. We do not send it out unsolicited.

Mr. FRANK. Do you call it to their attention? Do you call it to their attention? Come on. Don't play around.

Mr. HAWKE. If bankers' groups come through, it is among the materials that we distribute to them, but——

Mr. FRANK. Without soliciting——

Mr. HAWKE. You are not letting me answer the question, Mr. Frank.

Mr. FRANK. No. I resent that. You don't want to answer the question. Here's the deal: You are engaged in recruiting. This is part of your recruitment, and you don't want to acknowledge it. And, frankly——

Mr. HAWKE. No. I do acknowledge it.

Mr. FRANK.—you are better off acknowledging that you are recruiting.

Mr. HAWKE. I do acknowledge it, but you won't let me explain why we put this video together or how it is used or what it responds to.

Mr. FRANK. I was asking you how it was used. You sent it unsolicited——

Mr. HAWKE. What it responds to is, first of all, inquiries that we get about people who want to form banks and they want to know what the difference is between our charter and the State. Second, we send it to national banks when they ask us if we have any materials to respond to the very aggressive marketing efforts of State bank supervisors who personally get in touch with our CEOs and with boards of directors to try to market the State charter and induce conversion, which is something we do not do. We provide it to them on request——

Mr. FRANK. All right. You have given me two categories. One, you send it out to people who ask for it; two, you send it to national banks who ask for it. But there is a third category and you are just being evasive. Clearly, you have acknowledged you make it available to others. Yes, you and the State-chartered banks are in kind of a competition here.

Mr. HAWKE. I don't deny that at all.

Mr. FRANK. Okay. Well, you just tried to, I think, and I don't understand why it is appropriate for the Federal bank regulator—I mean you don't get paid by the bank, you are not on commission here. You are a regulator and I just think—and the problem I have is this, and I am going to close with this: If am the regulatee a competition between regulators to have me join up into their shop I think means, "Oh, gee, I have to look for who is going to regulate me the least."

I think it is counter to the public interest to have regulators in a competition. I will say the same thing to the States, but we don't have as much control over them. I do not think the Federal bank regulator ought to be competing with others to try and induce the regulatees to come be regulated, and I think that is a big part of our problem.

Mr. HAWKE. Well, I would invite you to look at the web sites of most State bank supervisors who very aggressively market State bank charters, and they do it in two ways. First of all, they exploit the Federal subsidy that is made available to State banks, because the Fed and the FDIC don't charge for examination services. That is exploited every day by State bank supervisors. Second, they advertise with kind of wink how close they are and how responsive they are.

Mr. FRANK. Let me just—I have one more. Why do you care? So some banks leave your regulatory jurisdiction and they go there. Just hurts your pride? I don't understand this, why are you in this competition with them, you said you are. Why aren't you just out there to regulate the banks that want to be national banks, and if they want to be State banks, that is also Okay? What is your institutional interest?

Mr. HAWKE. I think the essence of the dual banking system is competition between charters. That is what it is all about.

The CHAIRMAN. The gentleman's time has expired.

The gentleman from Iowa, Mr. Leach.

Mr. LEACH. Well, I would like to raise another question on the competitive regulation issue in another context in relationship to statute the House is advancing. The chairman of the Federal Re-

serve has argued that the lack of activity limits on and consolidated supervision of the organizations which own ILCs create competitive inequities in the financial marketplace to the disadvantage of traditional national bank charters and traditional State bank charters. Does the 28th Comptroller of the Currency agree?

Mr. HAWKE. Well, Mr. Leach, ILCs I know are an issue of great concern. It is not an issue that comes within our supervisory or regulatory involvement. The major issue with respect to ILCs is, obviously, as you said before, banking and commerce, which is an issue I know that you feel very deeply about. And the question that present is where to draw the line, a question that this committee has grappled with on many occasions.

I think it is certainly appropriate for Congress to consider not only that policy but the safety and soundness aspects of depository institutions affiliated with non-banking operations and also the competitive issues that are raised by that. As I say, we haven't really had occasion to take a position on this issue, because it is not something that comes within our regulatory jurisdiction.

Mr. LEACH. But do you see any competitive inequities?

Mr. HAWKE. Well, I think there are—any time you have a situation where an institution of that sort has powers that go well beyond those that are available for others, there is a potential for a competitive issue.

Mr. LEACH. So even though you have already indicated there is competition between State and Federal regulators, you don't think that the Comptroller should be deeply concerned that there are competitive inequities that affect institutions the Comptroller supervises or are you saying that they should? You are suggesting that the competitive inequities exist.

Mr. HAWKE. There are a lot of competitive inequities. We hear complaints from our banks all the time about competitive inequities with credit unions, for example, who have a status that enables them to compete very vigorously with our banks. If ILCs, by virtue of the lack of restriction on who can own them, had competitive advantages over national banks, I think that would be of concern to us. Well, I will just leave it at that.

Mr. LEACH. Thank you. No further questions.

The CHAIRMAN. The gentleman yields back.

The gentleman from Illinois, Mr. Gutierrez.

Mr. GUTIERREZ. Thank you very much, Mr. Chairman. I would like to go back to the preemption because sometimes lenders put clauses in their contracts to discourage borrowers from every pursuing legal claims. In fact, some lenders put clauses in loan documents that make borrowers agree that only certain courts can hear their claims—a lot of language sometimes when you get a car or buy a consumer product. And so they do everything they can so that the consumer can't go into certain courts. I think we all agree that that happens out there in the real world.

Well, in Georgia, they had an anti-predatory lending that tried to stop this practice, and that law was preempted by the OCC. For the life of me I can't figure out why the OCC would try to prevent Georgians from trying to protect themselves and their consumers and what the OCC would want to do in preempting a Georgia law

so that Georgians who are getting ripped off have different avenues that they can go.

And it seems to me that the Office of Thrift Supervision said that they did not believe they had that power to preempt the Georgia law on thrifts, yet apparently the OCC feels it has the same power that the Office of Thrift Supervision doesn't feel it has over its thrifts.

So I guess just following up on Mr. Frank's question is that I bet that if each of us, members of this committee, went back to their States—because, Mr. Hawke, there are 50 Attorney Generals, each one of them elected by the people of their State. These are law enforcement officers and all 50 of them said unanimously, "What Mr. Hawke is doing and the OCC is doing is affecting our ability as State law enforcement officers from carrying out consumer protection laws in our State." Pretty broad-based group of law enforcement officers.

If the 50, I don't know, Chicago police officers got together, I think you might think that was enough, but imagine New York and all of the police officers, LA, Chicago and all of our cities coming together to say, "Congress is doing something," not in this case, we are not doing anything, "but a Federal institution is doing something that impairs." Because it is a crime. I mean selling drugs on the corner is a crime, right? Mugging, rape is a crime. Murder is a crime. Predatory lending is a crime. So we should not somehow take these State Attorney Generals and these bank supervisors who are out there to fight crime.

And so it surprised me that when I read your opening statement that you said, "The OCC's mission is accomplished through three major programs: Supervise, charter and regulate." And nothing is said here about consumers and protecting the consumers. It is supervise, charter and regulate. And it wasn't until page 18 that I finally read something that spoke about consumer protection.

So I don't get it, Mr. Hawke, why we can't sit down and bring elected officials, Attorney Generals and bank supervisors who are appointed, much as you were, the President nominated you, you were confirmed by the Senate. Guess what, these bank supervisors at State banks are nominated by their respective governors and that is State government. You know, we always said here, especially I heard it a lot from my colleagues from the other side is, "Washington doesn't have the answers." They have the answers at the local level because they are closer to the people."

States' rights. You know, in this case, I think that is why Sue Kelly and Mr. Paul and I are working together. We do agree that when it comes to fighting crime, even if you, Mr. Hawke, increased and you are not increasing the number of supervisors you have. According to your testimony, you are decreasing the number of people you have. You have it right here in your testimony, you are decreasing the number. But let's say you were increasing it. Let's say I am wrong and I misread your numbers. If you have got 2,000 people fighting crime, why wouldn't you want 2,000 more, 1,500 more, 7 more, 5 more, so when I am affected by crime and 911 doesn't answer, right, which is OCC, 911, doesn't answer, maybe somebody at the local level will take this under their charge and help us fight crime.

Having said that, don't you believe——

The CHAIRMAN. The gentleman's time has expired.

Mr. GUTIERREZ. Has it?

The CHAIRMAN. It has indeed.

Mr. GUTIERREZ. Oh, God.

[Laughter.]

Mr. GUTIERREZ. Aren't you going to give the gentleman another minute to answer my question?

The CHAIRMAN. You are just getting on a roll.

Mr. GUTIERREZ. Well, don't you believe we can work out a cooperative agreement sharing jurisdiction with the States, preserving their authority to protect consumer rights? I think Mr. Hawke should be given 5 minutes to answer that 5-minute question.

[Laughter.]

The CHAIRMAN. That was a 5-minute question, 5 minutes plus, but we will——

Mr. GUTIERREZ. Well, if I were still the ranking member and this were held in my subcommittee, I would be given a little more latitude.

The CHAIRMAN. The gentleman may answer the 5-minute question.

Mr. HAWKE. Thank you, Mr. Chairman.

First of all, Mr. Gutierrez, our regulation does not preempt the arbitration clause in the Georgia law, so the concern that you have in that respect should be satisfied. Second, 911 does answer. It answers 70,000 times a year. We get 60,000 or 70,000 inquiries and complaints from customers of banks, many of which we refer back to other agencies or to the States. We have an extremely effective consumer complaint processing operation. Third, it is not us who is keeping State Attorney Generals out of national banks, it is Federal law that has been on the books for 140 years.

For 140 years, there has been a statute that says that the OCC has exclusive visitorial powers against national banks. That is to examine, to come into them, to take enforcement actions against them. That has been virtually unchanged. There are some very minor exceptions to it, none of which permits State attorneys general to come into our banks. As a matter of fact, 10 years ago when Congress passed the Riegle-Neal Interstate Branching Act, it reinforced that principle by saying that in the interstate branching context, State consumer protection laws, to the extent that they are not preempted, will apply to national banks, and the OCC will be the exclusive enforcer of those laws against national banks. So we operate in a statutory framework in which State law enforcement officials take enforcement actions against State banks and others within their jurisdiction and we take enforcement actions against national banks.

What is important here is not turf, not who takes enforcement actions against what institutions but how we arrive at coordination and a sharing of information. We have done that on many occasions. In the Providian case several years ago, we worked very effectively with local law enforcement authorities in California. We each worked within our own jurisdiction and we got $300 million in restitution against a bank while the State officials got restitution from the non-bank aspects of the company.

I mentioned the Security Trust Company case where we worked effectively with the State of New York and the SEC. If we can arrive at a modus operandi with State law enforcement officials where we refer matters back and forth within one another jurisdictions, we can be much more effective than we can if we are jousting about who has got jurisdiction over whom. The ability to send banking——

Mr. GUTIERREZ. I think, Mr. Chairman, the answer is, yes, you are willing to work out a cooperative agreement with States Attorney Generals.

The CHAIRMAN. The gentleman's time has expired.

The gentleman from Texas, Mr. Hensarling?

Mr. HENSARLING. Thank you, Mr. Chairman. I will table for the moment the whole question of the desirability of preemption, but since the question was raised by the other gentleman, can you give us in very precise detail the resources that the OCC has to perform the task of consumer protection? Is it fewer resources, is it more resources? What is it that the OCC has to engage in the exercise of consumer protection?

Mr. HAWKE. We have 1,700 bank examiners, and we have 300 bank examiners who are permanently and full-time on-site at our largest banks. We have over 100—and those 1,700 bank examiners work, many of them, in consumer compliance and consumer protection. We have 100 examiners who are dedicated entirely to consumer protection and compliance. We have several dozen attorneys in Washington and throughout the country who work on enforcement and compliance matters. And we have our Customer Assistance Group in Houston, which has 40 people working full-time, receiving tens of thousands of complaints and processing them very effectively and getting very good results for consumers.

There has been a misapprehension that the regulations that we put out in January are somehow going to result in a massive switch of responsibilities and a huge in-flow of work to the OCC. That is categorically not the case. Those regulations did not change anything in the environment that would cause the OCC to face a resource shortage because new matters are going to be referred to us of the sort that we didn't handle before.

Mr. HENSARLING. Although the OCC is principally known as the regulator of very large, some of the Nation's largest banks, in fact it is the community-based institutions, I guess, that make up the bulk of the banks that you regulate. There has obviously been a recent wave of consolidation. Should we in this committee be concerned about this increasing wave of consolidation as smaller banks appear to be gobbled up by megabanks?

Mr. HAWKE. Let me address the first comment first. It is true that of the roughly 2,100 banks that we supervise, an enormous number of them are community banks. Probably 85 percent by number or over 90 percent by number of banks are under $1 billion in size of our banks, and half of those are under $100 million in size. So we have enormous concern about the health of the community banking system in the United States, and the great bulk of our people are devoted to the examination and supervision of community banks.

In terms of mergers and consolidation, I think most of those acquisitions have not involved smaller community banks. The big attention-getting acquisitions have involved mid-size and large banks, and I think in many cases community banks have been the beneficiaries of some of those transactions. Because when a merger occurs it generally opens up new opportunities for community banks to demonstrate how much more effectively they can serve people in their communities than branches of large banks that are headquartered in far distant cities.

Mr. HENSARLING. One of the goals of Gramm-Leach-Bliley, I believe, was the goal of bringing down barriers to entry so that there would be increased competition in the banking arena, greater choices and hopefully the reduction of cost for consumers. Now that we have had several years of history, do you have any observations as to what extent the law has been working to indeed eliminate and lower barriers of entry?

Mr. HAWKE. Well, Gramm-Leach-Bliley certainly did lower some of the barriers. I think it is interesting that many of the opportunities that Gramm-Leach-Bliley opened up have not been taken advantage of. We don't see much interest in banking organizations, for example, getting into insurance underwriting. There are a few, but that has not been a big deal. And we haven't seen much in the way of investment banking firms acquiring banks. There is greater latitude for banks under Gramm-Leach-Bliley to engage in investment banking activities, but many of them were able to do that to a great extent even before Gramm-Leach-Bliley.

So while I would say that Gramm-Leach-Bliley potentially opened up opportunities, they haven't been taken advantage of to a great extent.

Mr. HENSARLING. My time has expired.

The CHAIRMAN. The gentleman's time has expired.

The gentle lady from New York, Ms. Velazquez?

Ms. VELAZQUEZ. I am supportive of the OCC's tough actions on national bank engaging payday lending, including the issuance of cease and desist orders and monetary penalties. However, I am concerned that some banks that may be looking in the payday lending business will look to other charter types. Do you believe that banks are actively gaming the regulatory structure to be able to remain in the payday lending business?

Mr. HAWKE. I have heard indications that some of the payday lenders that we essentially forced out of the national banking system have looked to other banks, and I know the FDIC is concerned that payday lenders may be looking to link up with banks that they supervise.

Ms. VELAZQUEZ. Can you tell me what can Congress do to further limit the ability of banks to establish payday lending affiliates?

Mr. HAWKE. Well, the problem has not been so much banks establishing the affiliates, it started with the payday lenders looking for a way to evade State laws by linking up with national banks and holding themselves out as agents for national banks under the preemption doctrine. We thought that was an abuse of preemption, and that was one of the principal reasons that we came down hard on those four national banks that had allowed their charters essen-

tially to be rented out to payday lenders. That was a clear misuse of preemption.

Ms. VELAZQUEZ. Many financial institutions rely on foreign companies to process customer data and staff call centers, you know, outsourcing of jobs. Gramm-Leach-Bliley required Federal banking agencies to set forth customer safeguarding standards, and the OCC has provided specific guidance in this area. How does the OCC standards protect customer information that is stored abroad?

Mr. HAWKE. That is a very important question and one that we are presently very much concerned about. As banks outsource data processing activities, for example, that involve confidential customer information, we want to make very sure that the same kinds of protections apply that would apply if the activity was conducted by the bank itself.

Ms. VELAZQUEZ. Does the OCC examine foreign facilities to ensure that they meet the OCC's guidelines, and how often are such examinations carried out? And are such examinations conducted by OCC staff?

Mr. HAWKE. I may be wrong about this, but I don't think we have occasion to try to examine overseas a foreign vendor that is providing services. If I am wrong about that, we will correct the record. There is in U.S. law authority for us to examine providers of services——

Ms. VELAZQUEZ. So what do you intend to do?

Mr. HAWKE. Well, I can't tell you—in all honesty, I can't tell you exactly where that stands. It is an issue that is being considered by our supervisory people right now in the context of the concerns about the outsourcing of operations that involve confidential customer information.

Ms. VELAZQUEZ. The OCC prohibits national banks from making home loans based predominantly on the foreclosure value of the collateral. It does not, however, address the more common practices of high fees, prepayment penalties, mandatory arbitration or loan flipping. As a result, the OCC standard may not be strong enough as lending institutions that charge excessive fees may strip away an owner's equity but may not actually result in foreclosure. Under the OCC standard, it is my understanding that these institutions will not be penalized for their actions. Given these potential shortcomings, can you comment on how the OCC's rules and regulations protect consumers against predatory lending practices?

Mr. HAWKE. Yes, I would be happy to. First of all, the underwriting standard that you described is, as I said earlier, I think lies at the heart of predatory lending. Everybody has got their own definition of predatory lending, but the essence of predatory lending, I believe, is the unscrupulous actions of non-bank mortgage originators who target the equity in people's homes and come and push credit out at very high prices that strip the fees out in the equity of the house. We have seen evidence of that not in the banking system but in the non-banking system. That is why we put such heavy emphasis on the underwriting standard. The underwriting standard is something that bank examiners can look at and deal with.

Now, as far as other practices of the sort that you mentioned, we have at the OCC pioneered the use of section 5 of the Federal Trade Commission Act, which deals with unfair and deceptive prac-

tices. And we have taken action against abusive practices of a number of sorts that don't involve predatory lending as such but that are unfair and deceptive. And we can go after situations where under all the circumstances we think a bank is engaging in unfair and deceptive practices.

The CHAIRMAN. The gentle lady's time has expired.

The gentleman from New Jersey, Mr. Garrett?

Mr. GARRETT. Thank you and thank you for being with us today. I am going to do the odd thing and agree completely with all the statements made from the other side of the aisle with regard to the preemption issue. That troubles me as well. That troubles me from the last hearing we had when Sue Kelly held a hearing. I think back to where we are today comes from where our founding fathers established this idea that there was—they were suspicious of the tyranny of a central government and a central bureaucracy. Always for a good cause is what the Federal Government may be doing but with over zealousness it may infringe upon the interests of the people back at home. The people back at home are closer to the issues. They are supposed to be the engines of innovation, as our founders had intended it, and now we are going to be, as far as I can see, stripping it of that right.

The questions are the same that I had back then, and I haven't heard either from scanning your testimony or hearing what you have said so far what is the harm that we are trying to address here? What is the exigency, what is the immediacy that we have to go forward at this point? What was the immediacy that we had to go forward or you have to go forward with the regulations when Sue Kelly and other members—I don't know if I was on that letter or not—but other members signed on to a letter asking for holding back on those regulations coming forward at that time? What is the exigency of going forward today? And why is it not the purview of Congress and not an agency to establish in statute as opposed to regulation?

Mr. HAWKE. Well, let me say, first of all, there is obviously a difference of view on this. We don't think we did anything radically new. We didn't expand the standards of preemption, we didn't expand the areas covered by preemption beyond what the courts have repeatedly said or what had been in earlier interpretations and rulings that we put out or that are embodied in the OTS regulations. I think there has been a lot of exaggeration about the effect of our regulations. All we did was to codify principles that are long-standing. They go back well over 100 years. We did not do anything new.

And one example of that is when we preempted the Georgia anti-predatory lending law, the Attorney General of Georgia was asked if he could take us to court and he reviewed the precedence and said that he didn't think there was a chance of beating us in court on that issue. What we did was completely in conformity with law, and it did not change the ground rules at all.

Preemption is a constitutional doctrine and whether we codified the preemption rulings in the regulation or not, these issues were going to come up in court. They have been coming up in court in wholesale numbers. We have had scores of litigations over the last decade involving issues of preemption. Our banks are faced with the uncertainty of litigation as they move into new products and

new markets, and we have been asked on dozens of occasions to give interpretations about the applicability of State laws, and the reason we put out our regulation is to try to bring some predictability and clarity to long-standing doctrines.

We did not intend to and we did not in fact change the basic rules of preemption or do anything remotely resembling what has been attributed to us. So I know there are differences of view on that. What we did has been, I think, grossly mischaracterized by many people, but what we did was completely in conformity with long-standing law.

Mr. GARRETT. You are correct, it is a constitutional issue, the issue of preemption, I guess, where some of us said that if the courts are making those determinations out there, that there should be or should not be in the certain areas, as defined—as the courts hear it, then some of us would feel that that final arbiter of the decision as to whether you are going to go forward and enforce the preemption should be a congressional decision as opposed to a regulatory.

I think I have a little bit of time just to go to one other point that was raised, and that is the issue of the confidentiality or the privacy of the information going overseas. And you gave an answer on it where you said you really couldn't speak to it exactly, and I don't want to put words in your mouth. Is that because no decision has been made, that it is still in the process, what you are saying, as far as dealing with it, or just where are we in the process of coming up to it, and when will we have a resolution to that part?

Mr. HAWKE. What I meant to say was I just don't have the information at hand. We will be happy to follow up with a supplemental submission. I know this is an issue that our supervisory people have been addressing. The standards that we have applied to our banks domestically with respect to protection of confidential information will apply, do apply to internationally outsourced activities. What I was unable to address specifically is exactly what our supervisory people are doing with respect to the examination of vendors overseas who are engaged in that. And this is a matter that is being discussed on an interagency basis.

The CHAIRMAN. The gentleman's time has expired.

Mr. GARRETT. And if you could provide us with that information.

The CHAIRMAN. Without objection.

The gentleman from New York, Mr. Crowley?

Mr. CROWLEY. Thank the chairman, and thank you, Comptroller, for being here today as well. Regarding the national standards for combating predatory lending, one issue by OCC prohibits national banks from engaging in unfair or deceptive lending practices. As FDC governs these issues, there is concern that OCC will not have the authority to identify or enforce any unfair or deceptive practices. Can you explain how OCC plans to identify, enforce and punish those national banks or their operating subsidiaries that engage in unfair and deceptive lending practices?

Mr. HAWKE. Well, we do have the authority and until we developed it, the concept has sort of been laying dormant whether we could enforce section 5 of the Federal Trade Commission Act. That is now very well-established and accepted by our sister agencies as well. We have instituted a number of actions against banks using

that authority under section 5 of the Federal Trade Commission Act to remedy unfair and deceptive practices.

Information comes to us through a variety of sources: Referrals from State law enforcement, our examination process and our Customer Assistance Group and just through the way it comes to the Federal Trade Commission itself. So I think we have plenty of resources to use that authority, and we see it as a very potent weapon in our arsenal when we deal with abusive practices at our banks.

Mr. CROWLEY. Thank you for that. Comptroller, there are been a great deal of concern expressed to my office and to myself among the State regulators, such as Attorney General Spitzer from my State of New York, that the new preemption codifying the OCC's recent regulations will lead to weaker protections for consumers.

My question deals with how the OCC will address that concern, and in answering the question if you can make reference to the First Tennessee case that Mr. Spitzer made example of. And in viewing that example, how does the OCC plan to rectify that plaintiff, particularly, and how do you plan to proactively ensure that that type of situation doesn't happen again? What type of penalty do you have in mind for First Tennessee if it is decided they committed unfair and abusive lending practices? And, finally, how do you plan to conduct the outreach to State regulators like Mr. Spitzer to address the concerns like the one Mr. Spitzer put forward in his lawsuit?

Mr. HAWKE. Well, I am delighted to answer that because I think this goes to the heart of how we cooperate with State law enforcement officials. I want to be a little bit circumspect in discussing a pending case, but we had a very, very similar case to the First Tennessee-First Horizon matter come up last year in another bank, in another State. It came into our Customer Assistance Group, and one of the people at the Customer Assistance Group called the examiner in charge at the bank that was having the problem. The examiner in charge walked down the hall to the consumer compliance person and said, "Get this fixed." And it was fixed overnight and immediately.

Virtually the same set of facts is involved in the First Horizon case. Attorney General Spitzer is using this as a vehicle for trying to establish a principle, but as soon as we learned about the complaint, which we did when he filed the lawsuit, they didn't come to us with a complaint, but as soon as we found out we called the bank and said, "Get this fixed," and it was fixed. The customer has been made whole, the problem is solved and really the case has really no vitality left to it. We have not taken any penalty action against the bank. This appeared to be the case of a bookkeeping foul-up at the bank and a rather obtuse reaction by some lower-level bank people when the matter was brought to their attention.

Mr. CROWLEY. In terms of the relationship between yourself, the offices and Attorney Generals, how will that work?

Mr. HAWKE. Well, I——

Mr. CROWLEY. See, I noticed in your answer there a little bit, I won't say resentment, but——

Mr. HAWKE. No, not at all. I had a——

Mr. CROWLEY. maybe a little hesitation between yourself——

Mr. HAWKE.——conversation with the Attorney General just a couple of days ago and emphasized the importance of our being able to work together as we did in the Security Trust case. He said he would like to come and visit and I look forward to that.

A year ago, we proposed to the State AGs that we enter into a memorandum of understanding for information sharing exactly like we have with the State insurance commissioners. And so far only one State has picked us up on that—the State of Maine. But we remain very hospitable to working out a modus operandi with the States that will allow us to share information and coordinate and cooperate on enforcement activities rather than trip over each other's feet, as we race to take competitive actions.

Mr. CROWLEY. Thank you, yield back.

The CHAIRMAN. Mr. Murphy?

Mr. MURPHY. Thank you, Mr. Chairman. I want to shift gears and go another direction and talk about the Basel court issues, as complex as they are. But are the regulators, you, the Fed, the FDIC, OTS, any closer to agreement on how to handle the operational risk issues in Pillar 2?

Mr. HAWKE. We actually have been together on that issue for quite some time. I think there was a perception that there was a deep gulf between us, and that largely stemmed from the fact that I alone among all members of the Basel Committee was arguing that operational risk should be treated under Pillar 2 rather than Pillar 1. I got nowhere with that argument and the Committee moved ahead to include operational risk under Pillar 1. We then spearheaded the development of what is called the advanced measurement approach under operational risk, and the Fed has joined with us and the FDIC. And we believe that is a very effective way of dealing with operational risk, and we are all together on that now.

Mr. MURPHY. There are still some things, though. The Federal regulators have undertaken efforts to ensure that banks have contingency plans to deal with these unforeseen loss issues, but they are costly and will result in pure losses in the event of a disaster. But Basel II requires an addition of mandatory regulatory capital charge to cover operational risk losses. Doesn't this result in some double charge of banks seeking to comply with Basel II and the mandates of the Federal regulators?

Mr. HAWKE. Well, I think the Committee has been cautious to try to avoid double counting and double imposition of capital. The operational risk rules should not result in double counting of capital as between operational risk and credit risk, although I suppose there are some opportunities for spillover.

Operational risk does exist, and we have seen examples of it, and our banks themselves hold capital against operational risk. So I think the basic concept of capital against operational risk is a sound one. The big question is how we measure it and how we calculate that capital, and I think we have made tremendous advances in improving the Basel proposal on that score.

Mr. MURPHY. Thank you.

That is all I have, Mr. Chairman.

Mr. BACHUS. [Presiding.] Who is next? Okay. I am sorry. We are going in order of, I guess, who first arrived, and I have Mr. Scott

next. The order on this side, just so as long as everybody will know, I have got Mr. Scott, Mr. Bell, Mr. Watt, Ms. Carson, Lee, Emanuel, Israel, Maloney, Lucas, Sherman, Waters, Moore, Miller and Clay.

Mr. SCOTT. Mr. Hawke, why has the OCC not responded and answered the letter from my banking commissioner, Mr. Sorrell, of August 21 regarding the preemption of the Georgia Fair Lending Act? It seems very strange that you took 6 months to go section by section and preempt the Georgia Fair Lending Act, and yet for 7 months you would not respond to the banking regulator's questions on issues regarding that issue. Why is that?

Mr. HAWKE. Mr. Scott, you raise an entirely appropriate issue. The first I learned that we had not answered the commissioner's letter was when the letter came in just a couple weeks ago, and I sent him a note back with profuse apologies, and I was chagrined upon that we had not answered that. It was not the way we usually do business. It was an unfortunately glitch and I am very sorry that occurred. That response should go out by the end of this week. And I very much regret that we didn't meet our usual response time.

Mr. SCOTT. But 7 months is a long time. There is a purposeful nature to 7 months. And it might be important to note that that March 9 letter was cc'd to me and other members of the Georgia delegation which might have prompted that response. What I would like and humbly ask of you, as we have this trouble with letters and that in the previous question and answer period with the gentleman from New York you mentioned that you had a conversation with the State regulator of New York, is that too much to ask that you could pick up the phone and to call our commissioner and have a two-way conversation much as you have done with other States, especially with the fact that our law has been preempted? Could you do that?

Mr. HAWKE. Absolutely, and I will.

Mr. SCOTT. Would you like to have his phone number? Could I give that to you?

Mr. HAWKE. I have got a crack staff who will find his phone number.

Mr. SCOTT. Well, please do that because that is very important to me. I am the only Georgia congressman, Democrat or Republic, serving on the Financial Services Committee, and my people in Georgia look to me to raise the issues and most importantly to get my State the respect that they deserve. And it would go a long way to helping that happen if you would be kind enough to pick up the phone and talk to Mr. Sorrell and to ask and answer questions and have that dialogue.

Mr. HAWKE. I would be happy to do that, and I couldn't agree more about the very unfortunate lapse in our process. I am deeply apologetic and I appreciate you raising it.

Mr. SCOTT. Very good. Let me ask you a second question on a broader issue. On the broader rule that you adopted on February 12, 2004, Mr. Hawke, let me ask you why did you decide to adopt your rule without a public debate on the issue before Congress since the rule was rigorously and unanimously opposed by the Nation's governors, State legislators, State attorneys general, State

bank supervisors and consumer organizations, and their comments urged public debate and congressional review?

Mr. HAWKE. Well, that is a question that we have addressed, and I want to start by saying emphatically that we intended no disrespect for this committee or its members. We received views on all sides of this issue. We had gone through an extensive rulemaking process in which comments were received a wide variety of commentators. We believed that the principles that were embodied in the regulation were not new despite the mischaracterization of the rule, that they were embodied in more than a century of precedence. We were seeing uncertainty in the marketplace, as I mentioned before, and that was impacting our banks' ability to serve customers.

We saw that in some cases these anti-predatory lending laws were impacting on the ability of our banks to provide good subprime credit in these markets. The secondary market was constricting and banks were moving out of markets. As I mentioned earlier, we were facing a high volume of litigation and inquiries about these preemption issues, and we felt that our banks needed guidance and that we needed to move ahead with that guidance.

And, finally, we thought that it was important that the predatory lending standard that we announced in the regulation go into effect and that that be out there so that banks would have—and I appreciate that people think we didn't go far enough with that—but that predatory lending standard that is in the regulation is something that nobody else has done and no other State or Federal regulators have done, and we believed it was important to get that out there and get that into effect.

Mr. SCOTT. But you can see why some of us in Congress feel that you are stepping on our bailiwick here. It is our responsibility to make the laws, to legislate. It is yours to regulate, and this kind of action certainly causes alarm on our side.

Let me ask you——

Mr. BACHUS. Thank you, Mr. Scott. Actually, I think you are probably about 2 minutes over.

Mr. Hawke, as you know, some of your critics have charged that the OCC was not being sufficiently responsive to consumer complaints about unfair or abusive practices at national banks and focusing particularly on predatory lending practices. Walk us through the process that the OCC follows when it receives a complaint that one of its institutions is engaged in possibly unlawful conduct or has otherwise mistreated one of its customers.

Mr. HAWKE. Well, complaints come in from a variety of sources. We get complaints that are discovered in the examination process, and we get a very high volume of complaints and inquiries that come in through our Customer Assistance Group—70,000 a year. Many of those don't relate to national banks and we kind of pawn those out to the responsible agencies. But that is one way that we learn about practices, and when complaints do come in the bank is contacted, the bank is asked for an explanation of its conduct, and if we find that the bank has engaged in abusive practices, the matter will get referred over to our supervisory staff, and it could form the basis of enforcement action. That is the way many of these things get started.

Others come up in the routine examination process. We will find that a bank is offering a product or engaging in an activity that reflects abusive practices, and we will take action against them. We have found in the area of credit cards, secured credit cards and like products that some banks are really engaging in unfair and deceptive practices, not predatory lending the way I would describe it, and we go after them. We have had a good record of getting judgments against them.

Mr. BACHUS. Have you received any complaints that national banks are engaged in predatory lending practices?

Mr. HAWKE. We have no evidence that predatory lending is a problem in the national banking system. Indeed, there are repeated statements by all of the State attorneys general that predatory lending is not a problem of regulated financial institutions and their subsidiaries, but it is a problem that exists in the unregulated financial community, the mortgage brokers and the unregulated originators of mortgages. The State Attorneys General have stated emphatically that they have not engaged in enforcement activities against banks and their subsidiaries on predatory lending, they have no evidence of it, and we have invited referrals from consumer groups and from State law enforcement people on predatory practices at national banks.

I should just add, Mr. Bachus, that last year we put out I think what is the most expensive advisory on predatory lending that any agency of the government, Federal or State, has put out. And I really commend those to the reading of anybody who is interested in predatory——

Mr. BACHUS. I am going to take your word for it till I hear otherwise. You have mentioned credit card complaints about credit cards. Is that the major area of complaints?

Mr. HAWKE. Since most of the credit card operations in the country are conducted in national banks, we do become the recipient of complaints from credit card customers.

Mr. BACHUS. Are those all funneled through the Customer Assistance Group?

Mr. HAWKE. Many of them are.

Mr. BACHUS. Some of them aren't, though?

Mr. HAWKE. Well, some we pick up in the examination process directly, but many of them come in through the Customer Assistance Group. And if find an unusual number of complaints about a particular institution, we will feed that back into the examination process to find out what is going on. And we did in one case a few years ago we noticed a spike up in complaints about a particular institution, and we went back to the institution and said, "What is going on?" The management of the institution didn't even know that they had a problem, and we were able to get that fixed in a way that was very beneficial not only to the customers but to the management itself.

Mr. BACHUS. What I am hearing, and let me ask you if you are hearing the same thing, I am hearing constituents complain that they will get their credit card bill and from the time they get it to the time they have to pay it is not 30 days, it is not 25 days, it is 14 days or 17 days or the cycle's been shortened. Are you getting a lot of complaints of that nature?

Mr. HAWKE. We have gotten complaints of that sort, and those issues have been addressed on an interagency basis in our account management guidance, a number of practices of that sort.

Mr. BACHUS. Have been stopped?

Mr. HAWKE. I can't represent to you that they have all been stopped, but we put out pretty strong guidance to our credit card banks to avoid abusive practices of that sort.

Mr. BACHUS. Has any enforcement action been taken against banks who may have been engaged in——

Mr. HAWKE. I am not aware of any enforcement action as such that we have taken against them, but in some cases it is like—our objective is to make clear what the ground rules are for our credit card banks. There are problems that are reflected in these consumer complaints, and we have had meetings with our credit card banks and told them that they have got to get these things fixed, because, among other things, they are inviting additional regulatory legislation that will impose a remedy on them that they ought to be concerned about.

Mr. BACHUS. And I can tell you that that is some of the most enraged calls that I receive that are received to me from other members of, say, the Alabama delegation or what they consider an arbitrarily short period to respond to the credit card bill coming in. And I would like maybe if you could supply me with what those guidelines are.

Mr. HAWKE. We would be happy to.

Mr. BACHUS. I think my time is—well, actually, is the light still on? Okay. All right.

Mr. Watt?

Mr. WATT. Thank you, Mr. Chairman.

Welcome, Mr. Hawke. I would have to say that I have listened very intently to your testimony this morning in very great detail and come away very disappointed in several respects. First is in your failure to acknowledge that the OCC has overstepped even in the face of all of the opinion of this committee that you have in fact overstepped. Second, in your insistence that what the OCC did was not a dramatic change even in the face of everybody in the industry saying that what you did was a dramatic change.

In your, to me, inconsistent positions that it was absolutely imperative that your predatory lending standards be announced and it be gotten into, that these standards be out there, yet the other side saying that everybody is saying that there is no problem of predatory lending with national banks, I am perplexed about that. Your statement that banks were withdrawing from markets yet doesn't seem to square with this notion that there was no problem of predatory lending.

And then your most recent statement, something about regulatory legislation, which to me—well, I guess it happens all the time that there is regulatory legislation. I think the problem that we are having on this committee is that you are setting standards here that we believe are the prerogative of Congress to set and that you are misapplying the standards that have been set.

I have looked at the wording of the Barnett case that set a standard which says prevent or significantly interfere with the national banks exercise of its powers. That is the language that the case law

uses. The rule that you put out says obstruct, impair or condition a national bank's ability to fully exercise its Federally authorized powers. Do you read those two statements, the legal standard that the court set and the standard that the OCC set in its rule, to be one in the same?

Mr. HAWKE. When you look at the whole string of Supreme Court and other Federal court precedence relating to preemption, and they go back well over 100 years, the language in our regulation reflects what has been said in those cases.

Mr. WATT. So you are saying that the language that I just read that those two set of languages say exactly the same thing?

Mr. HAWKE. Well, I think when you look at the Barnett case as a whole, it does talk about conditioning the exercise of powers. But this is an issue that goes back to——

Mr. WATT. Well, I understand that it goes back a long time, but I mean I think what you have done is—maybe all you were doing was codifying your thinking about it, but in the process of codifying it by regulatory standards you have certainly hit a bunch of nerves that nobody thought you were regulating in. Let me just point up one of those that is troubling to me.

One of the areas that your regulation says you are going to deal with is regulating abandoned or dormant accounts. Now, North Carolina has an escheat laws. Does the OCC have some kind of escheat law?

Mr. HAWKE. We did not affect escheat laws at all.

Mr. WATT. Well, what does it mean when you say regulating abandoned or dormant accounts?

Mr. HAWKE. Let me explain, Mr. Watt. There are two Supreme Court cases that deal with escheat laws, and the law is very clear, that state escheat laws apply at the national banks and are not preempted so long as they provide a due process opportunity for customer to raise—for the owners to raise claims.

Mr. WATT. So does that not condition a national bank's ability to act or does it significantly interfere with it? I mean which one of those does it do? I mean——

Mr. HAWKE. We made clear in the regulation that—the regulation simply reflects the Supreme Court precedent. Where there is no due process provided in the State law, it is preempted. That is what our regulation says, that is what the Supreme Court has said.

Mr. WATT. No due process in predatory lending law when we don't really have a predatory lending standard at the Federal level, and you have got to write a regulation that tells what the standard is?

Mr. BACHUS. I think he is talking about the escheat laws.

Mr. HAWKE. I am just talking about escheat laws.

Mr. WATT. Well, I am talking about the whole range of laws here. I am trying to figure out where it is in this context that the OCC feels like it has authority to start articulating what the law is at the Federal level when there is no law?

Mr. HAWKE. Well, Mr. Watt, I have taken an oath to support and defend the Constitution of the United States, just as every elected representative has, and I have to apply our best judgment about what the Constitution provides in the area preemption. These are constitutional——

Mr. WATT. So when the Congress tells you that you have overstepped and you have applied a standard that is different than what the Congress says is the standard, you are going to say, "Well, this is my standard, and I haven't overstepped. I am not doing anything dramatically different than has been my prerogative all along." Who is the OCC?

Mr. HAWKE. Well, I firmly believe that to be the case, that we have not done anything different, that we have not overstepped our bounds. We have been involved in dozens of pieces of litigation involving preemption issues over the years. We consistently win these cases. Our views on preemption are constantly reinforce by the courts. Congress, obviously, can change any of those rules, and I think that the States recognize that preemption is a well-established doctrine.

When the Georgia legislature passed the Georgia preemption anti-predatory lending law, they had a provision in it saying that if this law is preempted for national banks, it will also fall for State banks. And they were expecting, they were anticipating that the normal doctrine of preemption would preempt the applicability of that law for national banks. And the State Attorney General said that he didn't see any prospect of overturning our judgment on that score. So I don't think this was really a close issue in terms of whether we were reading the existing law correctly.

Mr. BACHUS. Thank you.

Ms. Kelly?

Mrs. KELLY. Thank you. First, I want to thank Mr. Oxley for his recognition of how important this issue is to the American people and for bringing this issue to the attention of the full committee. As you know, several weeks ago, this committee passed a resolution that expressed serious concerns with the rules the OCC had finalized.

And, Mr. Hawke, I want to thank you for fulfilling your promise to me that you would appear here. I thank you for appearing here today.

Mr. Hawke, I recently read an article in the American Banker in which you made some very dismissive remarks about the New York State Attorney General and banking superintendent relating to their concerns with these rules that you finalized on January 7. Your comments and what appears to be a dismissive attitude towards the concerns that we have in the banking structures of New York are not constructive and they make it very difficult for some members of this committee to have confidence in your stewardship of the OCC with regard to these regulations—one of the reasons why I have asked today for a GAO examination of the implications of your regulations on consumer protections as well as the process by which you arrived at these rules.

I hope that as we move forward in reviewing the OCC activities, you will demonstrate a greater recognition of the concerns expressed by the officials in my State and in these other States, as you have heard today, who genuinely believe that these regulations will have a negative impact on consumer protections and on the dual banking system.

Mr. Hawke, I would like you to answer a few questions and I want numbers only. No discussion because these are very simple

questions. How many full-time people does the OCC have specifically devoted to customer service?

Mr. HAWKE. We have got about 40 people who——

Mrs. KELLY. Full-time?

Mr. HAWKE. Forty full-time people who man our Customer Assistance Group in Houston, but that is not the only way we deal with it.

Mrs. KELLY. I didn't ask that. I asked for a number, sir. How many full-time people work on regulatory work?

Mr. BACHUS. Ms. Kelly, I think he is saying that he didn't know. That is not the total answer to the——

Mrs. KELLY. Well, I know what he is going to say, and so I have already discussed it with him and it is in his testimony if you look at the graphs.

Mr. BACHUS. I am just saying that he may—in fairness to the Comptroller——

Mrs. KELLY. Well, are you going to give me more time since you are taking my time?

Mr. BACHUS. I will. I will, Ms. Kelly, but what I am saying I think he was saying that is not all the people. I don't know if you were asking about——

Mrs. KELLY. Fine. Mr. Hawke, finish your answer.

Mr. HAWKE. My answer was that we have 40 full-time people at Customer Assistance Group who are the initial in-take for tens of thousands of customer complaints, and we have 1,700 examiners and 100 examiners who are devoted to consumer compliance.

Mrs. KELLY. Well, quite frankly, I asked you about customer service only, so you didn't need to amplify the answer.

Mr. HAWKE. They all deal with the resolution of customer——

Mrs. KELLY. I am only interested in what you have dedicated solely full-time to customer service. That is 40 people if I understood your answer. Now, how many people——

Mr. BACHUS. Ms. Kelly, he actually said that some of the other staff is——

Mrs. KELLY. I understand that, but I am trying to get at my next question, which is how many full-time people work on the regulatory work, just the regulatory work?

Mr. HAWKE. Well, I am not sure how to characterize that, Ms. Kelly. The——

Mrs. KELLY. Well, just give—how many people are in the regulatory work?

Mr. HAWKE. Lawyers who work on regulatory matters, my Chief Counsel advises me that we have got 20 lawyers who work on regulatory matters.

Mrs. KELLY. Thank you, Julie. How many people do you have working solely in enforcement?

Mr. HAWKE. We have got 100 compliance examiners who specialize in assuring compliance with consumer protection laws, the several dozen consumer protection laws that we have, and we have probably got a couple of dozen lawyers in Washington and throughout the system that work on enforcement and compliance cases.

Mrs. KELLY. I am going to wait for Julie to hand you that paper.

Mr. HAWKE. Well, Julie tells me I understated it. We have got 25 lawyers in Washington in enforcement and compliance, 25 more

in the districts and 10 others in consumer and community relations.

Mrs. KELLY. Okay. So it is 25 in D.C., 25 in the districts, and how many more?

Mr. HAWKE. Ten.

Mrs. KELLY. Ten, 10 more. Okay. What was the specific caseload for each full-time examiner last year?

Mr. HAWKE. I will be happy to provide that, Mrs. Kelly, in a follow-up. I don't have that number at my fingertips.

Mrs. KELLY. With this change, what will be the specific caseload for each full-time examiner this year?

Mr. HAWKE. Mrs. Kelly, there will be no change as a result of the regulations that we put out. And that is one of the great misconceptions about what we did. The regulations, despite the difference of views, and I respect the fact that our colleagues in the States have different views on this, our regulations codified the long-standing existing rules. They will not result in a significant—in any change in our workload. I think that is a specious argument that is being made by those who have an interest in attacking our position on preemption.

Mrs. KELLY. I would be interested, sir, in the number, and if you would break it down in terms of who is detailed to the national banks and who is detailed to operating subsidiaries. I would also like to know what the specific caseload is for every full-time employee assigned to your Customer Assistance Group.

Mr. HAWKE. We will be happy to provide that information.

Mrs. KELLY. I think that I may have an answer for that. I have an article here from the American Banker quoting Sheila Bair, a former Treasury Department official who is now a management professor at the University of Massachusetts. She states, and she may not be correct, which is why I was trying to find out if you had a different figure, she said the study says—her study says that the OCC has 921 consumer complaints for every full-time employee assigned to its Customer Assistance Group. I just didn't know what that number was that you have assigned. She also points out that the OCC has very high workloads for complaint processing. She says, and I quote, I think that does underscore that the OCC really needs to beef up their complaint-handling ability.

My concern here is we need to make sure that the people who are involved in our banking system, their customers, have answers to their questions and have their complaints handled in a timely manner. She quotes in the study that the FDIC has 111 complaints per person involved, and the Federal Reserve has 124. At 921 consumer complaints for every full-time employee, that is a lot. I don't know what number she is using there. I would like you to answer if you do know what the number she is using, and if you don't, if you can get back to me, I would appreciate it.

Mr. HAWKE. I would be happy to answer that question, because as much as I love Sheila Bair, she really does not know what she is talking about here. The numbers that she gives are relatively accurate. I am willing to accept that they are accurate. But she takes no account of the efficiency of these operations. If you take the 111 or 124 complaints per FTE that the Fed and the FDIC have, that works out to about 1 complaint every 2 days. That is what their

ratio is. And ours works out to about four complaints a day. So the people that we have processing cases in our Customer Assistance Group handle, on average, about four complaints a day, based on the ratio of complaints to full-time staff.

You can't simply take bare bones numbers like that and make conclusions about the quality of workloads or the need for more people. So I think it was gratuitous of her and uninformed to make the conclusion that she did. We constantly review the workload in our Customer Assistance Group. We review it in our budget process, we are presently looking at it. If the workload down there appears that we need more people, we will devote whatever resources are necessary to handle the workload. We have not had workload complaints about that operation. It has a highly efficient operation, it is highly automated, we have put technology to great use down there.

I think it is a world-class operation that ought to be a model for customer assistance groups any place, and we have invited our colleagues at the States to come down and look at it. Taking bare bones numbers of the sort that Sheila did and drawing conclusions about workloads is totally inaccurate and uninformed, and I am sorry that she jumped to that conclusion.

Mr. BACHUS. Thank you.

Mrs. KELLY. I think I am entitled to a little more time since I have been interrupted so often.

Mr. BACHUS. Well, actually, you are——

Mrs. KELLY. Mr. Hawke, I appreciate if what you said is true——

Mr. BACHUS. You are 5 minutes over.

Mrs. KELLY. Just let me finish, please, my sentence.

Mr. BACHUS. Well, I think the record is pretty clear——

Mrs. KELLY. I think that I am entitled to that.

Mr. BACHUS.——that he doesn't agree with Mrs. Bair's assessment of the complaint-handling capacity.

Mrs. KELLY. I think it will come as a bit of a stunning comment to the American Council of Life Insurers and the University of Massachusetts that you think that Ms. Bair is inaccurate in her numbers, which is why I actually wanted numbers from you and I would hope that you get back to the Committee and give us numbers to—if you think these are in error, give us some numbers that are not in error so that we can know what the facts are.

Mr. HAWKE. I am not disputing the accuracy of the numbers. She got those numbers from us. What I am disputing is the conclusions that she draw gratuitously from the numbers. I think the numbers prove quite the contrary, that ours is a very efficient operation and that when you look at the number of complaints per FTE at the other agencies and look at what that implies as to the number of complaints that they can handle during the course of the year, it averages out to about one complaint every 2 days. And I don't think that evidences a great deal of efficiency in the operation. Ours averages out about one to four and a half complaints a day, and I think that is because we run a very efficient operation.

Mrs. KELLY. Perhaps you could give us some numbers then. Thank you.

Mr. BACHUS. Thank you.

Ms. Waters?

Ms. WATERS. Thank you very much.

First of all, let me thank you for being here, Mr. Hawke. I appreciate the work you have done over the years particularly on payday loans and the effort that you have put forward, and that is very important to me. I am sitting here listening very carefully to my colleagues, and I think you are in a little trouble here. And I am wondering why you are pursuing this at all.

I am curious about a few things. You have cited your reasons for believing that you have the authority and it is based in the Constitution. You have explained to us you have all of these enforcement resources—1,700 examiners, 300 people on-site permanently and others. I think another group of 100 are involved with consumer protection and consumer complaints.

I want to know then, given all of that, how many national banks or operating subsidiaries have been cited by the OCC for engaging in abusive real estate lending practices? And I am asking that question because when we take a look at the web site, the OCC's web site lists only five enforcement actions taken against national banks for abusive consumer practices since 2000. Three of these actions involve credit cards, and two focus on small short-term lending. In contrast, State banking supervisors and attorneys general's offices brought thousands of consumer actions during this period. So how do you justify given all the resources, the authority this preemption that you are insisting makes good sense?

Mr. HAWKE. Well, I don't know what the thousands of actions are that the State AGs brought. We have seen very little evidence of State AGs bringing actions against national banks, largely because Federal law says that they don't have the authority to do that. I will have to get back to you on the number of actions against operating subsidiaries.

I think it is important to recognize that when we examine our banks we really don't distinguish between the bank and the operating subsidiaries in terms of the activities that they engage in. If a bank is engaged in the mortgage banking business and they carry it out in an operating subsidiary, we examine that as a unified operation. So if we take action, we may take action against the bank or we may take it against the bank and its subsidiary as well. But I——

Ms. WATERS. I am trying to find out where you have been effective or how you have been effective in this area. For example, I remember with Wells Fargo out in California there was a case brought by the State of California because Wells Fargo was charging interest before they registered the loans or something like that. And that was not an action that you discovered; that was an action by our State. And then I am looking at this Wachovia case here. That is an action by, I think, Connecticut and maybe one other State. So what are you doing? I mean——

Mr. HAWKE. The Wells Fargo action involved a statute that does not apply to national banks and was so held by a Federal court in California. The Connecticut action raises a similar question; that is, whether an operating subsidiary of a national bank is subject to the same preemption rules as the parent bank itself. That was involved in the California case, it is involved in the Connecticut case which is a pending decision now. There are two decisions in

California that have upheld our position on the inapplicability of that law that you referenced to national banks.

Ms. WATERS. That was brought to your attention by California, though; is that right?

Mr. HAWKE. It was brought to our attention I believe by Wells Fargo, because the issue arose as to whether that statute could constitutionally apply to a national bank. This is one of the reasons that we felt that it was important to codify these preemption principles in a regulation, because there is a great deal of uncertainty created by laws of exactly that sort, whether it applies to national banks or not. And in that case, there were two cases out there in which the court said that that law did not apply to national banks or their operating subsidiaries.

Ms. WATERS. Well, I guess what I am really getting at—and I understand how you can get involved with the question of who has the authority at some point. I guess what I am getting at is who is initiating the complaint with these kinds of cases? You say Wells Fargo. They may have come to you to ask about the authority, but I believe that it is the State of California to say, "Something's wrong here. You shouldn't be doing this."

Mr. HAWKE. The Corporation Commissioner raised that issue——

Ms. WATERS. Yes, of course.

Mr. HAWKE.——with the Wells Fargo Home Mortgage Company, and that raised the preemption question, whether that law applied. And it was determined that that law didn't apply, so there was no enforcement action taken in that case.

Ms. WATERS. The question remains, in my mind, whether or not—well, I am convinced that the State should not be preempted. I don't think you can do better than North Carolina, for example. I mean I wish every State could adopt the anti-predatory laws that North Carolina has adopted, and I think you would agree that there is nothing in your regs that could do any better than North Carolina. Wouldn't you agree to that?

Mr. HAWKE. No, I don't agree, with great respect, Mrs. Waters, because these laws and the North Carolina law is one example of this that have had adverse unintended consequences that I think all Members of Congress should be concerned about. They have resulted in and threatened further constriction of the availability of subprime credit—good, non-predatory subprime credit.

The subprime credit markets have expanded in recent years. They have been one of the reasons that home ownership in the United States is now at a record high level. Credit markets have opened up to people particularly in minorities that have not had access to credit before because of the advances in the subprime credit market. And what has happened with some of these predatory lending laws is that they have constricted the availability of subprime credit. When the New Jersey law was about to go into effect last November there was a story in the American Banker that said that subprime lenders plan to reduce their involvement in the subprime markets in New Jersey by 70 percent because of the New Jersey anti-predatory lending laws.

Ms. WATERS. Well, let me just say this, Mr. Hawke. We don't have time to debate it, my time is up, but I can tell you even though you give high praise to the subprime market, and some are

very good, some bankers are very good at this, but we have discovered that a lot of minorities who have gotten these subprime loans were eligible for prime loans anyway and should have been getting them anyway. I mean that is one of the things that is come out of this. And then, of course, there is the whole story of the foreclosures, and we don't have time to debate it at this time.

I guess my concluding remarks are that I think you are in trouble on this issue, and no matter what happens in the court, the Congress of the United States can still legislate and then whoever would like will try and rule it unconstitutional, but I think that is where we are headed.

Mr. HAWKE. I should just add, Ms. Waters that the question you raise about switching people to higher rate credit where they are eligible for prime credit is one of the issues that we addressed in our predatory lending guidance. That is something that we are concerned about, and we have admonished banks not to engage in that practice. And if we find that that is occurring, we will go after them.

Ms. WATERS. We will see.

Mr. BACHUS. Thank you. Thank you, Ms. Waters. It goes from one side to the other. I am just going to take about 30 seconds before I recognize Congressman Miller, though. But I will say this, not in the form of a question, but I think the best news that I have heard this morning, Comptroller Hawke, is that you don't have any evidence that any of the national banks are engaged in predatory lending practices. I think I am correct if that is what I heard.

Mr. HAWKE. That is what all the State attorneys general say.

Mr. BACHUS. That is right. And I have heard no evidence to the contrary myself, nor have I heard any today. I have not heard any members accuse any of the banks in engaging in those standards.

And I will say just for the record that my belief is that the preemption regulations issued in final form by the OCC in February contain strong standards for national banks to follow in avoiding predatory or abusive lending practices. Number one, there doesn't appear to be any, among the national banks, any predatory lending practices. That may prove to be wrong or they may start, but I think what you are telling this committee is that you have in place what you feel is sufficient assets and sufficient personnel to handle complaints and to process complaints and investigate them.

Mr. HAWKE. That is correct, Mr. Chairman. And, in addition, we have put out very strong, extensive admonitions to our banks, not only about avoiding getting involved in predatory lending but having policies to make sure—and controls to make sure that they don't purchase predatory loans that are originated by others. And there is no other banking agency that has done anything remotely comparable to that guidance.

Mr. BACHUS. Fine. Thank you.

Mr. Miller?

Mr. MILLER OF NORTH CAROLINA. Thank you, Mr. Hawke. You just said that what you have done has led to a diminution of availability of credit and subprime marketing to lower income borrowers. There was one study, I think, in Colorado that said that there was a diminished volume, but then there was a later study by the Kenan-Flagler School of Business, University of North Caro-

lina that said the only diminution in volume was of the bad loans, the ones that were being flipped repeatedly and that in fact, according to that academic study, that there was only a reduction of loans with predatory terms and that there was no restriction of access or increase in the cost of loans to borrowers with blemished credit.

Morgan Stanley, fairly reputable outfit, concluded a survey in 2001 that I believe was published, that the tougher predatory lending laws had not reduced subprime residential lending volumes in any significant way. Inside B&C Lending, which is apparently a leading trade journal, found that top North Carolina subprime lenders have continued to offer a wide variety, full array of products for borrowers in North Carolina with little or no variation in rate compared to other States. North Carolina commissioner of banks, Joseph A. Smith, said that they had not had a single complaint about the lack of available credit because of this law. The North Carolina bankers supported this law.

What is your authority for saying that North Carolina law had led to a diminished availability for credit to subprime borrowers?

Mr. HAWKE. Well, there are several studies that deal with the effect of the North Carolina predatory lending law, and there is some debate among the academics about the——

Mr. MILLER OF NORTH CAROLINA. Can you get those to me?

Mr. HAWKE. I would be happy to.

Mr. MILLER OF NORTH CAROLINA. Please, because I haven't seen them. I have been looking.

Mr. HAWKE. I would be happy to provide them. I think they are referred to in my written testimony, but subprime lending went down in North Carolina after the advent of the law compared to——

Mr. MILLER OF NORTH CAROLINA. Well, have you examined the North Carolina School of Business study? Have you examined that? Has anyone in your office examined that?

Mr. HAWKE. The so-called Stegman study. Yes, we have examined that very carefully. That has been the subject of a lot of criticism by third parties who have no ax to grind that it was methodologically flawed, because it dealt with securitizations and it didn't look at loan originations. I would be happy to give you——

Mr. MILLER OF NORTH CAROLINA. Please give me those studies. Please give me those studies. I would love to see it, because there seems to be a heavy volume on the one side saying that the law has worked, it has produced predatory terms but not the availability of credit, but in fact home ownership purchase money loans in the subprime market have increased. That is obviously the kind of money we want to make available. That is increased. And the only thing that is gone down is the volume of loans because of flipping and loans that have predatory terms.

There have been a lot of questions and a lot of testimony today about your resources for compliance and enforcement. Ms. Waters referred to thousands at the State level. The information I have got, and I know this doesn't apply to national banks, but the State bank supervisory agencies in 2003 initiated 20,332 investigations in response to consumer complaints, which resulted in 4,035 en-

forcement actions. How many enforcement actions did the OCC bring in 2003?

Mr. HAWKE. I will have to furnish that information to you, but in 2003 we did process 70,000 complaints from consumers, most of which got resolved without enforcement action because our Customer Assistance Group is very effective in getting remedies for individuals who raise questions. They solve every day thousands of problems that customers have raised with their banks.

Mr. MILLER OF NORTH CAROLINA. Okay. Please, if you could get me the number of enforcement actions, that would be very helpful as well.

And you also said you had ample rulemaking authority under section 5 of the FTC Act.

Mr. HAWKE. No, we don't have rulemaking authority under the——

Mr. MILLER OF NORTH CAROLINA. But you can apply that.

Mr. HAWKE. We can apply it on a case-by-case basis. The Federal Reserve has the exclusive rulemaking authority.

Mr. MILLER OF NORTH CAROLINA. All right. And my understanding is in the last 30 years since they have had that rulemaking authority that they have promulgated two rules pursuant to that authority?

Mr. HAWKE. Right. That is exactly why we moved forward to use our authority to issue cease and desist orders in individual cases without the benefit of a rule, and we have probably had—since we asserted that authority, we have probably had 10 or 12 cases where we have used that very effectively.

Mr. MILLER OF NORTH CAROLINA. Well, let me ask you about some specific practices that I know are happening right now and whether you regard those as being violations of—prohibitional unfair and deceptive trade practices. Single premium credit insurance is non-refundable.

Mr. HAWKE. I think you can't simply take a practice out of context and say without benefit of the rule that——

Mr. MILLER OF NORTH CAROLINA. So I am getting a firm maybe?

Mr. HAWKE.——it is automatically unfair and deceptive.

Mr. MILLER OF NORTH CAROLINA. All right. Moving on, we heard testimony in this room, 2 subcommittees of this committee, 2 days ago of lower income borrowers coming away from the closing knowing what they are getting, how much money they are getting at closing, knowing how much money they are paying a month but finding out sometime later that the page after page after page of legally gobbledy-gook amounted to something like $20,000 or $30,000 in points and fees built into the loan. And they have discovered that the equity in their home, their life savings when they tried to sell their home or when their children did when they died that their equity was largely gone, their life savings was largely gone. They didn't even know that it happened. Are you now pursuing any kind of advisory to prevent that from happening? Are you encouraging any rulemaking on that point? Do you think existing law prohibits it? What are you doing about it?

Mr. HAWKE. In our advisory on predatory lending, we identified a number of practices that frequently accompany predatory lending activities, and we told our banks that if we found any evidence of

it in the banks, we would come after them with remedial orders and restitution orders.

Mr. BACHUS. Okay. Thank you.

Comptroller Hawke, I am concerned that you have been here since quarter after 10, and that is a mighty long time for you to be in the chair. Mr. Israel and Mr. Gutierrez both want either 5 minutes or whatever. We have been going over. Do you——

Mr. HAWKE. I am fine.

Mr. BACHUS. You are fine. Okay. All right.

Mr. Israel?

Mr. ISRAEL. Thank you, Mr. Chairman, and thank you, Mr. Hawke, for hanging in for as long as you have. I do have a question for you. You dealt with it in a limited way prior. But before that I just want to clarify one important point. I was going to make this point in an opening statement but in the interest of the Committee's time, I deferred.

As you know, this is the only time that the full committee has met to address this issue, and during consideration of the budget views and estimates we were asked to vote on an amendment that questioned the OCC's ability to implement this rule under your budget. I supported that amendment because I am a blue dog and I believe in fiscal responsibility and budget accountability, and I believe that we have to make the budget process and your budget process as accountable as possible.

But I don't want anyone to interpret my vote on that amendment as opposition to the rule itself. I believe that there is a very strong case to be made that these regulations will help preserve the dual banking system. And without Federal preemption national banks would be subject to State and local laws and the distinctions between State and national banks clearly would disappear. And that was not Congress' intent in establishing Federal banking charters and a Federal regulator, which leads me to my question.

I have listened carefully to opponents of this rule as they have argued that it will in fact limit the effectiveness of State laws and consumer protections. I believe that I am a very strong advocate for consumers in my district and around the country. I also believe that different levels of government have different resources and capacities and capabilities to enforce consumer rules and regulations that offer the most vigorous and expansive protection of consumers. Everybody has their own tools and toolboxes and collectively that is the strongest mechanism for enforcing consumer protection.

Some have said that you do not have enough tools in your toolbox, that your toolbox just isn't big enough to protect consumers and enforce consumer protection laws and that it is impossible for the OCC and State regulators to work in conjunction with each other. You have dealt with that several, maybe hours ago, but you have dealt with that prior in this hearing.

I just want to ask you for the record to reassure me, as someone who believes strongly in consumer protection, that you have the numbers and the qualifications and sufficient resources to work with State regulators and to enforce the law and protect our consumers.

Mr. HAWKE. Absolutely. I have an absolutely strong conviction that we do. I believe that our resources are very significant. We

have a very rigorous budget process, and our budgets have been well-balanced. We have got all the resources we need to put into this. The issue is, I think, is how we best cooperate and coordinate with State officials so that we are not competing to see who can get to the court first on these issues but that we refer matters back and forth.

We have the ability with bank examiners—bank examiners have a special relationship with banks, and when a bank examiner comes into a bank and says, "I want you to fix something," they get—by and large, they get very quick responses. And it is a lot more effective for us to use the examination process to cure some of these problems than to have somebody go into court and initiate a proceeding that is going to drag on for years at great expense to everybody.

So if we could find a modus operandi where if Attorney General Spitzer has a complaint, for example, against one of our banks or a subsidiary of our bank, if he would let us know about it instead of filing a lawsuit, we could get the matter fixed, as we did in the case that is presently pending. I think cooperation is the best way to achieve what we all want for the protection of consumers.

Mr. ISRAEL. OCC currently has how many employees?

Mr. HAWKE. We have got about 2,800 employees.

Mr. ISRAEL. How many are bank examiners?

Mr. HAWKE. Seventeen hundred are field examiners. We have another couple hundred who are in management positions.

Mr. ISRAEL. Thank you, Mr. Hawke.

And I yield back the balance of my time, Mr. Chairman.

Mr. BACHUS. Thank you, Mr. Israel.

Mr. Gutierrez?

Mr. GUTIERREZ. Thank you very much, Mr. Hawke, for being with us here this morning. I guess I just want to go over a few things and then, once again, implore you and your good offices to sit down with everyone and work this stuff out, because I just want to make it clear and put it on the record that you cite your authority as being 140 years old, going back to the Civil War and the National Bank Act. And as I shared with you in my office, if that were true, then you would be guaranteeing the money that the Mint today produces as really a one dollar bill, a five dollar bill. You no longer do that, nor do you have that authority. The Mint has that authority.

And I guess I would be writing to you and your examiners on April 15 because you would have the authority under that law to collect my taxes. But I don't deal with you or your bank examiners, although I might like that to be the case that I would be audited. I think you would probably be a fair arbiter of what my taxes would be.

And I mean it would be so sensational, Mr. Chairman, Mr. Bachus, that if you were representing Alabama, citing the Bank Authority Act, you would be calling President Jefferson Davis and I would be calling President Lincoln. That is how far back this goes in terms of what you are citing. Obviously——

Mr. BACHUS. I don't think we had telephones back then.

Mr. GUTIERREZ. I am sorry.

Mr. BACHUS. I don't think we had telephones back then.

Mr. GUTIERREZ. You would be riding on a horse and so would I to call our respective presidents of this country.

So I think that is pretty old precedent. Things have changed since then, and the authorities you had and that you cite under that act have changed dramatically. Well, I don't know that I would pay my taxes to you under that legislation nor did the Federal Reserve banks and board exist at that time. Things have changed and our Federal banking system has changed since then.

And so we can argue and debate the merits of one thing or another, but there is a quote from the Wall Street Journal, which Mr. Frank has put in the record, that says, it is a quote of you, "It is one of the advantages of a national charter, and I am not the least bit ashamed to promote it." So I know you promote national banks. I guess as a former representative of a local where we think we do things well, that is at the State level, whether it is Illinois or Georgia or North Carolina, we think we do things well.

Can't we not—because I believe that the Congress has shared with you, and many congressmen from both sides of the aisle have shared with you this morning and on various other occasions that we disagree. So there are a couple of options when you have a disagreement, right? One is that Congress can take actions, which you have said, "Please go ahead."

But I think that reasonable people—because I want to say this for the record: I think what the OCC does is a great job. We are not here to say you are not doing a great job. But I think there are other institutions that can help and that States now have abilities to help the consumers. It is not an either-or. Maybe it is a plus-plus situation. You know when they used to say English as the official language, I said, "No, English-plus. Let's learn French and Spanish and every other language."

And in this case, it is kind of like the OCC-plus, and if we could work out among ourselves in a deliberative, conscientious manner, then there isn't the need for hearing, we can all go about what we need to do, and I think you would be strengthened by having the support of both sides of the aisle, whether it is in the Senate or in the House, to do the job that I believe you want to do, which is to regulate and keep the safety and soundness of our national banks and hear from us about our consumer issues.

Maybe if Attorney General—I am just thinking—Attorney General gets a complaint, shares it with you, 30 days later unresolved, he pursues it. I don't know how we do this, but I am sure we can work out rules in which you can preserve the integrity of the institution that you were nominated and confirmed to protect, and we can do our jobs in terms of helping our States and our consumers be better served. That is my point.

Mr. HAWKE. Mr. Gutierrez, I completely agree with the importance of coordination and cooperation. We strongly believe I that. The table that I passed out earlier shows that de facto is an enormous clearing mechanism that is working every day. Complaints that are received in our Customer Assistance Group if they don't belong to us, they get referred back to the right authority. Complaints that go to the States are referred to us. Last year, we had 6,500 complaints referred by State authorities to us. We think that we can work very effectively together.

It is true things have changed in 140 years, but one thing that hasn't changed is the constitutional principle that was first announced by the Supreme Court in 1819, which is that the States do not have the constitutional authority to restrict the powers that Congress has granted to Federally created entities. Congress has the power to change that——

Mr. GUTIERREZ. I understand that, but I think there is—again, and we have had this discussion before, we can argue, right, about what Congress said and didn't say and so Congress can then say, "We disagree with Mr. Hawke, so, therefore, we are going to legislate this way." That could give this Congress work that maybe some feel it should have, but I think that among reasonable people—because I want to make it absolutely clear: I have stated that I think that what the OCC does is wonderful. I don't have problems with my nationally chartered banks. In my community, most of them they are good, honorable, hardworking people that go out every day and proactively search for lending products for those underserved communities. So I will say that in terms of the banking community. This is not a fight about the banking community. This is a fight about who is going to do that.

So all I would say is I will write a letter to the Attorney General. I will say, "Please, all 50 States, and to all the 50 States, all the bank examiners in those 50 States, please tell me where the OCC preemption on this issue affects consumers." And we will start that as a point at which your staff, our staff, I will be involved, others can get involved to resolve this. You win, States win, we resolve the issue, and we move forward. That is all I am trying to do here today.

Mr. HAWKE. If we can provide more effective protections for consumers, we are eager to pursue that course. And I think the best way to do so is by continuing to coordinate and exchange information with the State law enforcement authorities.

As I said before, a year ago we proposed a memorandum of understanding that would facilitate exactly what you are talking about, and so far we have had only one response to it. The State of Maine has agreed to it. Nobody else has even come back with comments on it. So we are eager to find a modus operandi that will make sure that we are all informed about what is going on in the banking system and that we are taking steps to protect consumers most effectively within our respective jurisdictions.

We have very awesome powers, and when we send bank examiners into a bank we can get results. We can fix problems before they become systemic. We can get nationwide remedies if we find systemic problems. I think we far better enforcement barriers than our colleagues at the State level in respect of dealing with banks.

Mr. BACHUS. Thank you.

Comptroller Hawke, just following up, and I am not going to ask you questions, but one thing I would be interested in is do most consumers, most homeowners know about the complaint resolution system? I mean is that information prominently displayed in——

Mr. HAWKE. It is. And, Mr. Bachus, I think the best evidence of that is the fact that we get 70,000 calls a year. Many consumer groups post our 800 number on their web sites. The number gets around, because we get 14,000 to 15,000 complaints a year that

don't even belong to us, and we farm those out back to the responsible agencies. So people find their way.

And one of the things that we can do with better coordination with the States is to make sure that if there is any question about where a complaint should go that we take steps to make sure that it gets to the right place.

Mr. BACHUS. Thank you. Let me ask one final question. One thing I want to do just for the record is you stated several times in this hearing room and other venues that you are very concerned about the state of Basel II, the negotiations and the complexity of those. I am going to submit some written questions to you concerning that in the interest of time, but I do want to end with this question. Comptroller, we have heard from some industries but in particular the check cashing industry. The banks have dropped them as customers as a whole industry. They just came in and said, "We are not going to have check cashers as customers anymore," even though there were no individual problems with individual check cashers. And they cite an OCC policy that they need more scrutiny than other businesses. And I think I have talked to you about this, and I think that they may be at a higher risk for money laundering, at least that is one of the things that is offered.

And my question to you is, and I have looked at the guidelines on the high risk and what is—and attorneys, car dealers, jewelry stores are all considered by our government as in that same category. But I have not heard from any car dealerships, I have not heard from any attorneys, I have not heard from any jewelers that any of their businesses have been dropped by banks. And I am concerned that there is discrimination or unreasonable interpretation of those guidelines, maybe by individual examiners. Would you like to comment on that?

Mr. HAWKE. I can't say that I know for sure, Mr. Chairman, exactly what the complaints are about the check cashers. I know that when I was at the Treasury Department there was an issue about the linkages between check cashers and banks with respect to direct deposit.

Mr. BACHUS. Yes. That is a different issue, I think.

Mr. HAWKE. The issue here, I suspect, relates more to money laundering, and I would say that we have done nothing that should have resulted in banks dropping check cashers as a class, and I think that is one of the things that has to be looked at on a case-by-case basis.

Mr. BACHUS. And I would like you to be aware of that, because these are the legitimate licensed businesses. And I might disagree with certain type of businesses, but I think they have the right to have national banks and to—so I would appreciate you looking into that.

Let me close by saying that you have been subject to a rigorous examination here this morning, and I personally think you have acquitted yourself very well. You have been under a long examination, and I think your answers have been candid, I think they have been open, and I very much appreciate your testimony here this morning. And although I may not be the one that should be offering an apology, I think on at least one or two occasions you were treated somewhat shabbily by members, and I apologize for that.

Mr. HAWKE. Mr. Chairman, I appreciate the interest and involvement of this committee. These are important issues and there are no easy answers, but I welcome the opportunity to try to clarify our view of the implications of what we did, because I think there have been some significant misstatements and exaggerations about the impact of our regulations.

Mr. BACHUS. All right. And I think that you were vigorous in pointing that out. And I think you have maintained dignity in a high degree of professionalism, and I thank you for that.

Mr. HAWKE. Thank you, Mr. Chairman.

Mr. BACHUS. With that, our committee is dismissed.

[Whereupon, at 1:07 p.m., the Committee was adjourned.]

APPENDIX

April 1, 2004

Opening Statement

Chairman Michael G. Oxley
Committee on Financial Services

"Oversight of the Office of the Comptroller of the Currency"
April 1, 2004

The Committee meets today for the latest in a series of oversight hearings we have planned for this year on the Federal agencies under the Committee's jurisdiction. Last month, the Oversight and Investigations Subcommittee, under Mrs. Kelly's leadership, held a hearing on the operations of the Federal Deposit Insurance Corporation. Today we turn our attention to the Office of the Comptroller of the Currency, the independent agency within the Treasury Department that charters, supervises and regulates the more than 2,000 institutions that make up the national banking system.

We are pleased to have back before the Committee the Honorable Jerry Hawke, who has recently returned from a brief medical leave to resume his duties as the Comptroller of the Currency. Comptroller Hawke, we welcome you back, and we wish you a continued speedy recovery.

In addition to reviewing the operations and regulatory policies of the OCC, today's hearing provides an opportunity to take stock of the health of the national banking system. Last week, the OCC released its report on the condition of national banks in the fourth quarter of last year, reflecting net income 21 percent higher than for the same period a year ago, markedly improved credit quality, and record numbers for both return on equity and return on assets. Even with all of the shocks that our economy has undergone over the past four years – beginning with the bursting of the tech bubble in 2000 and continuing through 9-11 and the scandals in corporate America – the fundamentals of the U.S. banking system appear to have never been stronger.

This surely bodes well for the sustainability of the economic recovery that has begun to take hold in recent quarters, as banks with sound balance sheets are well-positioned to make the kinds of loans to creditworthy borrowers that can help to fuel growth and create jobs.

One by-product of the record profitability that the banking industry has enjoyed in recent years has been an increase in merger activity among some of the country's largest institutions, including, within the past six months, three supervised by the OCC – Bank of America, Fleet, and Bank One. While the trend toward consolidation in the financial services industry is not a new phenomenon by any means, these most recent mergers nevertheless raise important issues regarding the future structure of the banking industry.

As the primary Federal regulator for the nation's largest and most complex banking organizations, the OCC faces a particular challenge in maintaining an examination force with the technical expertise necessary to ensure that these institutions are operated safely and soundly while continuing to meet the needs of the communities they serve.

Since its inception 140 years ago, the national banking system has offered banks that operate on a multi-state or nationwide basis the ability to do so under unified Federal supervision, and pursuant to one set of rules established at the national level. This fundamental principle, which has been reaffirmed in numerous Supreme Court opinions, has come under fire in recent months from opponents of regulations issued in final form by the OCC in February that seek to codify the supremacy of Federal law as applied to national banks.

As a state legislator for nine years before coming to Congress, I do not dismiss lightly the claims by state banking commissioners and others that the OCC regulations undermine the dual chartering regime that has been a hallmark of the U.S. banking system since Civil War days. However, I simply cannot agree with my friends in the States that subjecting national banks to a patchwork of inconsistent standards set by State legislatures and local municipalities is either required by the dual banking system **or** in the best interests of the customers of those institutions.

In January of this year, Mrs. Kelly's subcommittee held the first congressional hearing on the OCC's preemption regulations. The hearing was a fair and balanced look at this complex issue, at which the OCC and its critics were both afforded opportunities to state (and defend) their positions. Since then, the OCC has taken several constructive steps to address legitimate concerns expressed by Members and witnesses at that hearing. On March 1st, the OCC issued guidance to national banks stating the OCC's expectation that when national banks or their operating subsidiaries receive customer complaints forwarded by State authorities, they must take appropriate measures to resolve those complaints fairly and expeditiously. Then last week, the OCC published a proposed rule that, once fully implemented, will result in a full listing of all national bank operating subsidiaries being available to the public over the Internet, to facilitate the processing of consumer complaints against such entities. I applaud the OCC for taking these important steps, and I encourage the agency to continue to reach out to its state counterparts to address areas of common concern.

Before I conclude my remarks, let me say a few words about Basel. This Committee remains extremely concerned about the potential competitive impact that the Basel proposals might have on the U.S. banking system, and about the continued lack of consensus among federal banking regulators regarding the merits of the proposal.
I will be particularly interested in hearing Comptroller Hawke's views on studies released recently by other Federal banking agencies addressing both the competitive issue and the potential effect of the new Basel framework on the prompt corrective action regime that applies to U.S. banks.

I now recognize the Ranking Minority Member for an opening statement.

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April 1, 2004

Statement of the Honorable Rahm Emanuel
Committee on Financial Services
Hearing on "Oversight of Office of the Comptroller of the Currency"

Thank you, Mr. Chairman, for holding this important hearing. These issues are of great concern to officials in my home state of Illinois, who are worried about the impact these rules will have on consumers and small businesses.

While I commend the Office of Comptroller of the Currency for including two new requirements in the final rule intended to address potential lending abuses by national banks, I am concerned about taking the local "cop on the beat" off the street, especially in light of the fact that national banks now have thousands of local operating subsidiaries in major cities like Chicago.

I also believe OCC may have inappropriately applied its preemption standard to exempt from state laws the operating subsidiaries of national banks – even if these operating subsidiaries are *state-chartered* entities.

And I think a strong case can be made that federal preemption should be debated and decided by Congress. An example of this is the recently enacted FACT Act (FCRA) that preempts several state laws. This was done only after a full and complete debate by Congress and a majority decision that is appropriate in this area. The bipartisan FACT Act process should serve as a model for considering issues of federal preemption going forward.

I understand that Ranking Member Barney Frank and the State Attorneys General have called on OCC to voluntarily narrow the scope of these rules, and have told OCC that if it does not act by May, he will introduce a resolution of disapproval under the Congressional Review Act.

I look forward to hearing from Comptroller Hawke today, and to working with my colleagues to ensure a vibrant dual banking system that encourages competition and protects consumers from abusive predatory lending practices.

Thank you, Mr. Chairman.

April 1, 2004
Statement of Congressman Gutierrez
OCC preemption hearing

Good morning. I would like to thank Sue Kelly, my Oversight Subcommittee Chairwoman, for originally calling this hearing, a follow up to our hearing on January 28. I am pleased that Comptroller Hawke has recovered from his illness and able to join us here today and work with us on this issue. Due to the great interest in this issue, this has become a full committee hearing.

I would also like to thank Ms. Kelly and Mr. Paul for their work on this important issue of OCC preemption. We are committed to working together with a number of our other colleagues on both sides of the aisle, including Ranking Member Frank, to ensure that our states have the power to protect consumers.

And to stop the OCC from eroding strong safeguards that have been used by the states for more than a century to enforce consumer protection laws.

It makes no sense to me that the OCC would attempt this misguided, unprecedented, unchecked expansion of its authority, when the states currently have the tools and resources to effectively enforce consumer protection and other important laws.

As many of you know, since our last hearing in January, Rep. Ron Paul and I passed an amendment to the Financial Services Committees Budget Views expressing concern regarding the budgetary effects of the OCC's recently published preemption rules. The budget views now put the Financial Services Committee on record that the OCC's preemption rules represent an unprecedented expansion of authority, and one that was instituted without Congressional authorization.

We were particularly concerned because the Administration's budget projects OCC spending as increasing only 2 percent from fiscal year 2004 to fiscal year 2005, and provided no staffing increases in FY 2005.

In fact, Mr. Hawke's prepared testimony today indicates that the number of full time employees and bank examiners, in particular, have steadily declined each year over the past three years.

The OCC seems to believe it can function under a budget that is virtually the same as when it didn't have this vastly increased portfolio of regulatory responsibilities.

This means the OCC would have to divert resources from mission critical functions or fail to enforce these consumer protections as diligently as the states have done.

Alternatively, they could significantly increase their bank examination fees, which provide their revenue, but I don't think they (or the banks they serve) are eager for that to happen.

We were pleased that the Committee agrees with us on this important issue and we look forward to continuing to work with our colleagues in Congress as well as the state Attorneys General and others who share our concerns.

I think it is clear that we will never agree with the OCC regarding the authority it purports to have. We may simply have to put it aside as a philosophical difference.

It is more important that we clearly define what responsibilities should remain with the states, including the right of attorneys general to protect their citizens by litigating against banks who violate state laws. I have, in fact, urged the Comptroller to sit down with the Attorneys General and other state regulators to work out some form of cooperative and shared jurisdiction, including state licensing and the applicability of state consumer laws to national banks and their operating subsidiaries. I would hope that some agreement would be reached so that further Congressional action would be unnecessary.

In the meantime, Chairwoman Kelly and I have asked the GAO to investigate and examine the OCC's conduct relating to the finalization of these rules as well as the impact of these rules on the dual banking system. I will eagerly await their report on these issues, and, more immediately, I look forward to the testimony of Comptroller Hawke here today. Hopefully it will be as entertaining as his recent remarks to the American Banker on this issue. Thank you.

Congressman Steve Israel
Opening Statement, House Financial Services Committee Hearing
Oversight of the Office of the Comptroller of the Currency
April 1, 2004

Good morning. First I would like to thank the Chairman and Ranking Member for holding this important hearing this morning. The issue of the recently finalized OCC regulations have been hotly debated both here and in many of our State Capitols. It is important the Congress take the opportunity to weigh in. I would also like to thank Comptroller Hawke for appearing today – I look forward to hearing your testimony.

Mr. Chairman, I will be brief, but I do wish clarify a few points that I feel have been clouded during the course of this debate. First, as you know, this is the only time the Full Committee has met to address this issue. During consideration of the Budget Views and Estimates, we were asked to vote on an amendment that questioned the OCC's ability to implement this rule under their budget. I supported that amendment. As a fiscal conservative, I feel strongly that we must make the budget process as accurate as possible.

However, that vote should not be interpreted as opposition to the rule itself. I believe that there is a strong case to be made that these regulations will help to preserve the dual banking system. Without federal preemption, national banks would be subject to state and local laws and the distinctions between state and national banks would disappear. This was not Congress's intent in establishing federal banking charters and a federal regulator.

States have an important role to play in regulating state-chartered institutions, but do not have the authority to regulate the activities of national banks. That is the basis of the dual banking system.

Beyond the need to guarantee a strong dual banking system, these regulations will ensure that national banks are able interact with consumers on a uniform basis, no matter where the consumer is located. They also permit national banks to offer products and services more efficiently and conveniently.

I am looking forward to hearing the Comptroller's testimony today as well as to a vigorous discussion of these and other issues. Thank you Mr. Chairman, I yield back the balance of my time.

STATEMENT

PETER T. KING
before the
COMMITTEE ON FINANCIAL SERVICES

April 1, 2004

Thank you, Chairman Oxley.

Comptroller Hawke, I would also like to welcome you to the Committee and certainly look forward to your testimony.

As a Representative from New York, I have a strong interest in protecting the banking and consumer protection laws enacted in my State. That is why I joined several of my colleagues in letter to you, dated December 1, 2003, expressing concern with your proposal to exempt national banks from most state laws.

The rule, which went into effect February 12, 2004, could have profound implications on our duel banking system and enforcement of consumer protections in the states. Preempting state regulatory and enforcement laws is a serious action that, in my opinion, should be examined by the Congress and not enacted through regulation.

I do, however, believe the OCC has touched upon a serious issue important to this country's system of banking. The expansion of national banks across state lines offers consumers financial products that may not be available within their particular state. Although I believe this is beneficial for consumers, reconciling the desire for uniform consumer laws with strong consumer protections should be addressed legislatively.

In addition to the forum where this decision should be made, I am concerned about the consumer protections afforded under this rule in lieu of the protections enacted at the state level. Specifically, I am curious to see how the OCC matches the resources of state banking departments, consumer credit divisions and offices of state attorneys general that work to identify fraud and abuse.

Increasing your portfolio of regulatory responsibilities will certainly strain your budget. I hope this does not force the OCC to divert resources from their other responsibilities, or fail to enforce consumer protections as diligent as the states.

Lastly, I am interested in hearing an update on the Basel negotiations. As you know, the Basel Capital Accord establishes the amount of capital internationally active banks must hold in relation to various assets on their balance sheets. There is concern that, as drafted, Basel II could adversely impact competition, is overly prescriptive, and mandates excessive capital charges for operational risk. You have called Basel II "mind-numbing in its complexity" and "complex far beyond reason." I hope you will expand upon those remarks and discuss the concerns Basel II presents to the US banking industry.

Thank you again, Comptroller Hawke, for your participation today and I yield back the balance of my time.

For Release Upon Delivery
10 a.m., April 1, 2004

TESTIMONY OF

JOHN D. HAWKE, JR.

COMPTROLLER OF THE CURRENCY

Before the

COMMITTEE ON FINANCIAL SERVICES

Of the

U.S. HOUSE OF REPRESENTATIVES

April 1, 2004

Statement Required by 12 U.S.C. § 250:

The views expressed herein are those of the Office of the Comptroller of the Currency and do not necessarily represent the views of the President.

I. INTRODUCTION

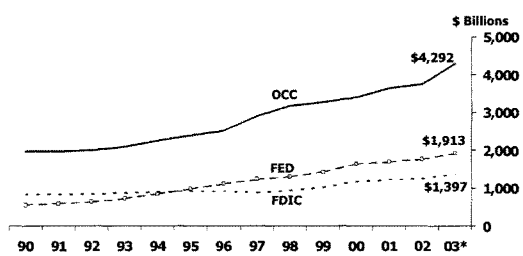
Mr. Chairman, Ranking Member Frank, and members of the Committee, I appreciate this opportunity to review the condition of the national banking system and the state of the Office of the Comptroller of the Currency (OCC). My written statement covers three principal areas. First, I will report to you on the current state of the national banking system, which is sound. Second, I will describe how the OCC strives to manage our financial resources efficiently and deploy our human resources effectively to ensure that the national banking system maintains its sound condition and its vital role in our country's economy.

The third section of my statement highlights three areas of our work that are of central significance to the way national banks will conduct business in this new century. There, I will describe our risk-focused approach to supervising the national banking system. I will also provide an update on the progress of the ongoing international and domestic deliberations about prospective revisions to the Basel risk-based capital framework. Finally, I will highlight the importance of an attribute that is key to the national bank charter – the ability of national banks to operate under uniform, nationwide standards, consistent with Federal law – and I will try to correct what I believe are some fundamental misunderstandings on several points concerning the regulations we have recently issued on applicability of State law to national banks and their operating subsidiaries. I also want to reiterate our willingness to work cooperatively with State officials on referrals and resolution of customer complaints, and identification and timely response to any inappropriate practices by the institutions we respectively supervise.

II. THE CONDITION OF THE NATIONAL BANKING SYSTEM

The OCC supervises federally chartered national banks and federally licensed branches of foreign banks. As of year-end 2003, the national banking system consisted of approximately 2100 banks (26 percent of all commercial banks). Of these, approximately 2000 were FDIC-insured banks, holding total assets of $4.3 trillion (56 percent of all commercial banking assets). The rest were uninsured bank and trust companies. The OCC also supervises 53 Federal branches of foreign banks. While the number of national banks has declined for nearly two decades, the national bank share of total system assets has remained roughly constant. The national banking system includes many

Assets by Federal bank supervisor



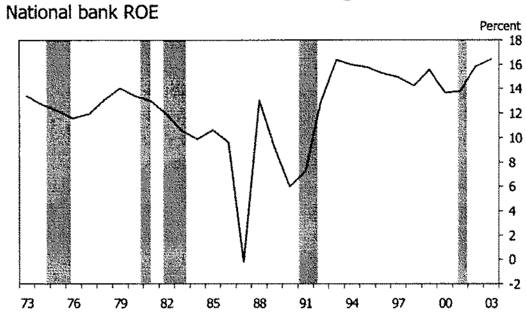
Source: Integrated Banking Information System (OCC). *Data as of December 31, 2003

of the largest banks by asset size, but community national banks are by far the most numerous in the system.

The financial performance and condition of the banking system is strong. Bank earnings have remained at historically high levels for a decade. Until 2002, aggregate net income for national banks had never exceeded $12.5 billion in a quarter, and the industry's average return on assets had never exceeded 1.5 percent, at least not since the quarterly reporting began in 1984. But since the beginning of 2002, national banks have exceeded both earnings milestones in every quarter but one. In 2003, national banks set new records for both return on equity and return on assets. Although the slow economy led to weakness in some areas, including business lending, the contractions in these areas were more than offset by growth elsewhere.

National bank ROE at record high

National bank ROE



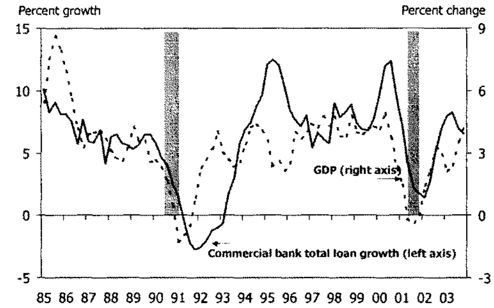
Source: Integrated Banking Information System (OCC)

Data as of year-end. Shaded areas represent periods of recession.

Total loans held by banks continued to expand throughout the recent economic cycle, growing by 7.8 percent in 2002 and 7.6 percent in 2003. In contrast, starting with the recession of 1990-91, total loans held by national banks fell for 10 consecutive quarters. Where the earlier recession affected all sectors of the economy, the recent recession was concentrated more extensively in the business sector, in part due to the fallout from the tech/telecomm bubble in the late 1990s. This caused a sharp fall in the demand for business loans, particularly at large banks.

The reduction in corporate lending by banks also was due to the competitive influence of the low rates on corporate bonds. Many large and even medium-size firms have been able to access the bond market at very low rates throughout this economic slowdown, which has further reduced the demand for larger commercial loans. This has affected especially the lending activity at the largest banks, because they tend to have potential business customers who have greater access to other financial options. Community banks, however, taking advantage of their knowledge of local markets and business needs, have maintained their business lending throughout this cycle, with increases reported in their commercial and industrial (C&I) and commercial real estate loan books.

Loan growth continued throughout this recession



Source: Integrated Banking Information System (OCC); BEA/Haver Analytics

Quarterly data through Q2-2003. Shaded areas represent periods of recession.

The mortgage and consumer sectors have been a strong source of loan growth for national banks. Residential real estate loans held by national banks rose at an annual rate of about 20 percent in both 2002 and 2003. Within this broad category, home equity lending has grown particularly fast, rising by 21 percent in 2001, 38 percent in 2002, and 37 percent in 2003. Throughout this cycle, consumers have taken advantage of the declining mortgage rates to extract funds from the increased value of their homes. Some of these funds from the refinancing and home equity loan activity have been used, however, to pay off higher interest credit card and installment debt.

The low interest rate environment has been a plus and a minus for banks. Smaller banks with their greater reliance on retail funding have seen steady erosion in their net interest margins. By contrast, the largest banks, which rely more on wholesale funding, until recently experienced relatively high net interest margins. As of December 2003, the net interest margin for banks in all asset size groups has fallen below their historic averages. Despite the decline in margins, banks have reported continued growth in net interest income due to the strong expansion in household lending. As long as margins remain compressed, however, this growth in income is vulnerable if volume of activity in the consumer markets falls.

The low interest rate environment also raises concerns about the extent to which banks may be taking on interest rate risk in an effort to maintain their interest income. Effective management of this risk will be important for banks in all asset size groups as the economy recovers, which is often accompanied by an increase in interest rates. We have alerted national banks to our concerns on this score and provided advice on approaches on how best to address this "low rate set-up."[1]

Deposits have continued to flow into banks, especially large banks, as might be expected when low interest rates hold down returns on alternative money market instruments. Deposits at national banks grew at 6.0 percent in 2001, 7.6 percent in 2002, and 8.6 percent (year-over-year) in 2003. The increase in deposits has fueled growth in bank assets. The assets of national banks grew 9.8 percent in 2003 (year-over-year), as compared to a 0.1 percent decline reported at this point of the recovery from the last recession. Nevertheless, we believe banks must be vigilant in their assessment of the potential sensitivity of their sources of funds to changes in the economic

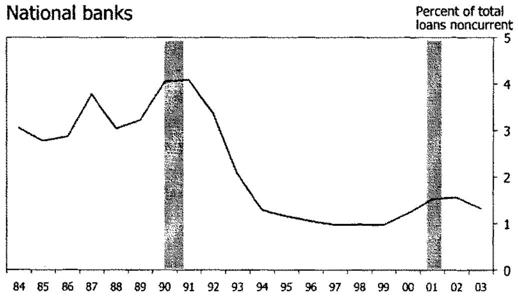
[1] OCC Bulletin 2002-19, "Supplemental Guidance on Unsafe and Unsound Investment Portfolio Practices," May 22, 2002.

environment or, in some cases, the bank's own performance. The high level of liquidity in the banking system could be reduced rapidly if the relative yield on alternative investments increased sharply or if banks failed to maintain certain performance levels required to retain some sources of funds.

While credit quality deterioration is typically an issue during recessions, the most recent experience for national banks was much better than during the previous recession. This may well reflect national banks' response to cautions issued by the OCC to bankers in the late 1990s to be vigilant about their underwriting standards. The noncurrent loan ratio for national banks (loans at least 90-days past due plus nonaccruals) reached a peak of 4.4 percent in 1991Q2; in contrast, at the peak in this economic cycle, reported in 2002Q2, the noncurrent ratio was 1.6 percent. For large banks (over $1 billion in assets), the noncurrent loan ratio has now declined to 1.3 percent, near pre-recession levels. Smaller banks (under $1 billion in assets) were not as affected by the stresses in the nonfinancial corporate markets and thus experienced only a modest decline in credit quality during the recession. While credit quality appears to be improving for the banking industry, the OCC continues to watch developments in areas that remain vulnerable, such as small business lending and certain real estate markets and property types.

Noncurrent loans remained well below level of early 90s

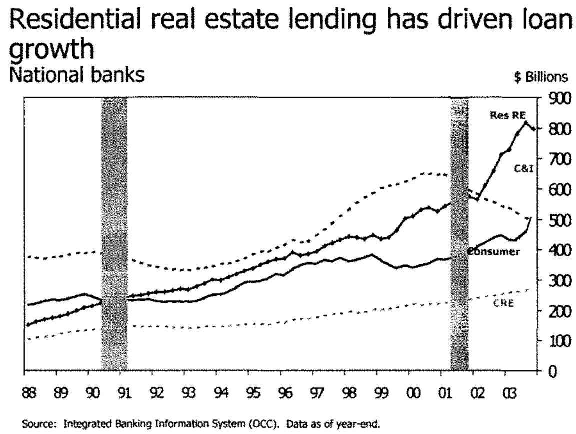
National banks



Source: Integrated Banking Information System (OCC) Data as of year-end. Shaded areas represent periods of recession.

The data on failure and new entrants to the commercial banking system also reflects a very dynamic and healthy banking system. In 2003, two banks failed – one national and one State bank. By contrast, 100 commercial banks – including 33 national banks and 67 state banks – failed in 1992, the first year of recovery after the 1990-91 recession. The commercial banking system also had 111 new entrants in 2003; this compares to 40 new banks in 1992.

Banks' business strategies have continued to evolve in response to demographic shifts, changes in technology, and improvements in risk management. Larger banks have moved increasingly into retail lending during a period of strong growth in demand from the household sector. Large banks have benefited from their geographic diversification, and have captured economies of scale by moving to automated processing of standardized products like home mortgages. Small national banks have seen more modest growth in retail lending. Economies of scale are reflected in the continued improvement in the efficiency ratio for large banks (noninterest expense to net operating revenue), a factor that also has contributed significantly to overall bank performance in recent years. In contrast, small banks have expanded their business lending, where many continue to find profitable niches offering customized products in local markets.



While the national banking system has displayed strong performance, even during the recent recession, history teaches that we cannot know for certain what lies ahead, and banks' capital provides important protection against that uncertainty. National banks remain well capitalized and rest on a much firmer capital base than they did a decade ago. In 1990, for example, 6.3 percent of banks had risk-based capital ratios below 8 percent, which we would now consider undercapitalized, and 18.3 percent were below 10 percent. Today, all national banks, with the exception of a few small banks under special supervision, have risk-based capital ratios above 8 percent, and more than 90 percent of national banks have risk-based capital ratios above 10 percent.

III. <u>THE STATE OF THE OCC</u>

The OCC's mission is accomplished through three major programs: supervise (including risk analysis), charter, and regulate. The OCC is headquartered in Washington, D.C., operates the Ombudsman's office in Houston, and maintains district offices in Chicago, Dallas, Denver, and New York. The agency has 48 field offices and 23 satellite locations in cities throughout the U.S., has stationed resident examiner teams in the 24 largest banking companies supervised, and maintains an examining office overseas in London. The agency has approximately 2,800 employees, the vast majority of which are bank examiners. To accomplish our mission in FY

2003, we used 2,761 Full-Time Equivalents (FTEs), down slightly from 2,792 in 2002, and 2,837 in 2001. Total examiner FTEs were 1,837 in 2003, 1,853 in 2002, and 1,888 in 2001.

The OCC receives no appropriated funds. Our funding is derived from assessments and fees and we set our budget each year based on agency practices and our estimation of available revenue for the upcoming year. Our budget has been balanced during all the years that I have served as Comptroller, and we have the resources available, as needed, to assure that we fulfill all dimensions of our responsibilities as supervisor and regulator of the national banking system. We guard against potential disruption to our operations due to major, unpredictable events affecting our funding, for example, through a contingency reserve that is funded on an incremental basis as part of the budget process, each year.

Effective supervision of a dynamic national banking system in a changing financial services marketplace demands careful management of our financial resources and thoughtful deployment of the first-rate work force we have been able to attract. In recent years, the OCC has placed a heavy emphasis to improving the discipline with which we manage our financial resources and building enhanced accountability into the way we manage our human resources.

Improving Financial Performance

For the past five years, the OCC's financial management initiatives have been strongly focused on improving the planning, budgeting and program evaluation processes; strengthening financial accountability and internal management controls; and modernizing our financial operating systems. The OCC maintained its "green" rating – the highest of three possible ratings – on the Financial Performance Initiative[2] and received from its external auditors, Gardiner, Kamya, and Associates, an unqualified opinion on its FY 2003 financial statements with no material weaknesses. We have received an unqualified opinion on our financial statements for 39 consecutive years. We close our books within three days of month-end each month, and our independent auditors are able to issue their audit report by November 15th each year.

Our ongoing commitment is to ensure that timely, accurate, and relevant management information is conveniently available to OCC program managers. Over the past five years we have improved the OCC's planning, budgeting, and program evaluation process in major respects. Since the first quarter of FY 2002, we have employed quarterly budgeting and implemented a procedure that requires advance approval for significant reprogramming actions. During FY 2003, we developed a five-year variable projection model that uses revenue, budget, reserve target, and actual reserve projections to allow management to better understand the financial impact of their business decisions on the future operations of the OCC. For FY 2004 we have adopted a new activity-based accounting code structure that will assist OCC managers in making staffing decisions and ensuring that resources are used in alignment with the OCC's strategies.

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[2] The Financial Performance Initiative is one of the five initiatives in the President's Management Agenda. The Office of Management and Budget scores the progress of each agency toward accomplishing these initiatives using a green/yellow/red scoring system. The Department of theTreasury scores its own bureaus, including OCC, in a similar fashion.

We have in place a strong quality management program that employs regular reviews and special studies designed to foster continuous organizational improvement. The OCC's program analysis unit evaluates program efficiency and effectiveness, and assists management in ensuring that OCC programs are strategically aligned with our objectives. The combination of administrative funds control processes and a strong management control program help us ensure that we maintain integrity and accountability in all of the OCC's programs and operations.

We recently upgraded our financial management and acquisitions system ($MART) to web-based technology. $MART is a state-of-the-art system that is Joint Financial Management Improvement Program (JFMIP)- and U.S. standard general ledger-compliant. The system has allowed us to integrate the budget execution function with the core functions of accounts payable, accounts receivable, asset management, and general ledger. $MART provides users with on-line access to daily status of funds and financial performance reports, and it provides appropriate security over financial information. Utilizing the features in $MART and management information provided by our new activity-based accounting structure, we expect to continue making progress throughout FY 2004 in further integrating budgeting and performance management and program evaluation.

Responding to New Management Challenges

The OCC supports the Department of Treasury's 2003-2008 strategic goals of promoting prosperous U.S. and world economies; preserving the integrity of financial systems; and ensuring professionalism, excellence, integrity, and accountability in the management and conduct of the Department of Treasury. The OCC has established four strategic goals to achieve its mission and contribute to the achievement of the Department of Treasury's strategic goals. The OCC's goals, as defined in our 2003-2008 strategic plan, are a safe and sound national banking system; a flexible legal and regulatory framework that enables the national banking system to provide a full competitive array of financial services; fair access to financial services and fair treatment of bank customers; and an expert, highly motivated and diverse workforce that makes effective use of OCC resources. Described below are initiatives we have undertaken in two key areas that present cutting-edge management challenges.

Expanded e-Government and IT Security

The OCC developed a three-year plan to fully implement the Clinger-Cohen Act and capital planning best practices. The plan was implemented in FY 2003, and significant progress was made during the FY 2004 budget cycle. The FY 2004 capital planning process significantly increased the involvement of all OCC business units, and training was provided on the capital planning program, e-Government initiatives, and the OMB's business case development.

We have recently implemented web-based interaction with national banks, including optional electronic filing of an increasing number of applications and electronic notification to banks of consumer complaints received by the OCC Ombudsman. The OCC also has recently deployed phase one of the automated learning information center for OCC employees, a state of the art learning management and delivery system. We are now initiating phase two, which includes the

development of operational, management, and integrated reporting capability. The learning management system is becoming a model for other agencies.

In the area of IT security, the OCC created a computer security incident response center to monitor, respond, and report to Treasury regarding virus attacks, intrusion attempts, and other security incidents. We have integrated security considerations into capital planning and system development processes, and inventoried all information-processing systems and grouped them for certification and accreditation. The OCC has also improved our continuity of operations by implementing an IT recovery strategy that is commensurate with the threats and risks of the post-9/11 era.

Emergency Preparedness

Immediately following the terrible events of 9-11, we established a Contingency Planning Oversight Committee to conduct a comprehensive review of the OCC's emergency management program and contingency plans. The committee was tasked with analyzing the existing program and plans to determine what changes were needed to address new and emerging threats. The result of the committee's work was the development and implementation of a Continuity of Operations Plan that ensures the OCC can respond to any emergency impacting our operations and can continue to perform essential functions necessary to support the mission of the OCC and the banking and finance sector of the nation's critical infrastructure. We recently re-organized our critical infrastructure protection and security functions into a new business unit to continue focusing on this work and allow the OCC to begin performing an even greater role in the planning and coordination activities of the banking and finance sector.

During the past two years the OCC completed a comprehensive physical risk assessment of our headquarters facility and implemented new security procedures and security systems at our key facilities. We also developed, implemented and tested new Information Technology disaster recovery strategies for those key information systems and applications necessary to support the OCC's essential functions. In addition to our physical and information assets, we also focused on the protection and safety of our most important asset, our employees. The OCC was one of the first Federal agencies to issue survival kits to all employees and one of the first to develop, implement and successfully test shelter-in-place procedures. We have also developed a testing, training and exercise plan that allows us to educate and prepare employees and which also enables us to identify and correct weaknesses in our contingency plans and emergency operations.

Positioning our Workforce for the Future

The most important asset the OCC has is its people. One of the challenges we face is to ensure that the structure and expertise of our workforce continues to evolve as the national banking industry changes. The OCC restructured its district offices last year by combining the existing six district offices into four offices to better realign our workforce with the location of the banks we supervise. We have managed these efforts carefully to maximize the choices available to employees affected by the restructuring and to minimize disruption to our ongoing operations and loss of critical expertise.

This past year, the OCC completely re-engineered its recruitment processes by hiring a professional recruiter as a permanent member of our staff and placing greater emphasis on a centralized approach to college recruitment. These changes have resulted in the hiring of a diverse cross-section of top quality candidates. To ensure that these candidates will be able to carry on the OCC's tradition of excellence for years to come, we have improved our training for pre-commission examiners and renewed our emphasis on employee retention. Retention efforts are particularly focused on new hires, who are especially susceptible to turnover during their first four years with the OCC.

For more than twenty years, the OCC has operated as a performance-based organization with a strong emphasis placed on aligning individual performance expectations with organizational priorities. Annual pay increases granted to employees are based on the extent to which their performance objectives are met rather than on cost of living changes or longevity. We offer compensation and benefit programs that are tailored to achieving several goals, including matching the diverse needs of our workforce, supporting the several components of our mission, and controlling costs so that we can continue to operate within a balanced budget.

Because our ability to fulfill our mission depends on the skill, dedication and good judgment of our people, we strive to maintain an environment that promotes creative and thoughtful contributions and encourages diversity of viewpoints. It is a measure of our success that the OCC was recently recognized as one of the "Best Places to Work in the Federal Government" in a report released by the Institute for Study of Public Policy Implementation.

IV. Keeping Pace with Change in the National Banking System

Change is a consistent theme in the operation – and the supervision – of the national banking system today. National banks must evolve their businesses if they are to remain competitive in today's financial services markets. At the same time, the OCC must adjust its supervisory and regulatory approaches in order to ensure that national banks can avail themselves of all of the attributes of their charter safely and soundly. Among the most important strategies we have developed to maximize the effectiveness of our examination and supervisory program is our risk-focused approach to supervision.

The OCC's Risk-Focused Approach to National Bank Supervision

OCC's supervision by risk approach dates back more than 10 years and involves supervisory policies and processes that tailor our oversight to the key characteristics of each bank, including asset size, products offered, markets in which it competes, and the board's and management's tolerance for risk. This process provides an effective means for the OCC to allocate our supervisory resources and to better communicate to senior bank management the areas where they may need to correct problems before they become entrenched.

Risk-based supervision begins with an assessment of a banking organization's existing and emerging risks, and management's efforts to manage and control those risks, in nine specified risk areas: credit, liquidity, interest rate, price, foreign exchange, transaction, compliance,

strategic, and reputation. Based on that assessment, the OCC examiner-in-charge or portfolio manager will develop and implement a detailed, supervisory strategy for the bank, based on its risk profile and the complexity of its lines of businesses. Examiners identify areas of highest risk, understand exactly what management is doing to address those risks, and communicate regularly with management to indicate where additional management actions are needed. In performing this evaluation, OCC examiners consider not only the activities of the bank and its operating subsidiaries, but also how the bank's risk profile is affected by the activities of other subsidiaries and affiliates.

Our assessment of the integrity and effectiveness of a bank's risk management systems includes appropriate validation through transaction testing. If this produces concerns, we will "drill down" to test additional transactions. If this reveals problems, we have a variety of tools with which to respond, ranging from informal supervisory actions directing corrective measures, to formal enforcement actions, to referrals to other regulators or law enforcement. The examination procedures implementing OCC's supervision by risk program are documented in the Comptroller's Handbook.

Supervision by risk provides an effective way to supervise banks in the current rapidly changing environment. It also allows us to apply a consistent supervisory methodology across an increasingly diverse group of banks and bank activities. Because the design of this approach requires that we customize an examination based on a bank's underlying risk characteristics, it allows us to more effectively direct OCC resources to the banks or activities within banks exhibiting the greatest risk.

In response to the growing divergence in the complexity and scope of operations between large and small banks, we have divided our day-to-day supervisory operations into two lines of businesses – our Community and Mid-size Bank program and our Large Bank program.

Our Community/Mid-size Bank line of business oversees over 2,000 national banks and Federal branches and agencies through our network of district, field and satellite offices. When examining this population of banks, examiners use a core set of examination procedures to draw conclusions about the magnitude of risk and the adequacy of the risk management system for each of the nine areas of risk. Even in low-risk banks, we sample, verify, and test the bank's policies, procedures, and systems. When risks are elevated; when activities, products and services are more complex or present greater financial or compliance risks; or when issues or problems emerge, examiners will expand the scope of their supervisory activities using more detailed guidance found in topical booklets of the Comptroller's Handbook series. Periodic monitoring of community banks, another key element of the supervisory process, is also designed to identify changes in the bank's condition and risk profile, including new products or services, and to assess bank corrective action on outstanding supervisory concerns between formal onsite examinations. This quarterly monitoring process allows examiners to identify significant changes in the risk profile of the banks they supervise on a timely basis.

Our Large Bank program focuses on the 24 largest national banks. The supervision of each large bank, overseen out of our headquarters office, is staffed by a resident examiner-in-charge and a team of examiners and specialists in areas such as commercial and retail credit, capital markets,

bank technology, asset management, and compliance. These examiners and specialists track the quantity and quality of risk management in real time so that our assessments are forward-looking as well as historical. This program allows the OCC to develop a more thorough knowledge of the bank than is possible through the traditional regime of periodic, discrete examinations. Over the years, we have also developed, tested, and refined this supervisory approach expressly to address the special financial and compliance challenges posed by bigger, more complex, and globally positioned banks. We are confident that this approach will be effective to supervise the "mega-banks," those will assets of a trillion dollars or more, that are forming as a result of recent acquisition activity in the industry.

Today's national banking system operates not just nationally, but globally. Our large banks all have operations or a presence overseas. Our London office provides us with examiner expertise to interact with foreign supervisors and provides a platform to examine national bank branches overseas. Our London examiner staff provides a critical network to deal with home/host country issues, information sharing issues, and outsourcing issues. We also participate in the Foreign Banking Organization program (along with the Federal Reserve Board) to examine and supervise Federal branches and agencies in the United States.

We also are deeply involved in the development of international bank supervision policy through our participation in the Basel Committee on Banking Supervision and in the Joint Forum, which is an international group of banking, securities, and insurance supervisors; through our regular dialogue with foreign banking regulators; and through our international and technical assistance programs that provide training and internship opportunities to bank supervisors. In fact, not long ago we detailed to the Treasury Department four experienced examiners who are now working in Iraq.

To help meet the challenges of an ever more complex banking industry, our resident and field examiners and specialists are supported by a team of policy specialists, analysts, accountants, and economists in our headquarters office who monitor industry, market and economic trends, provide technical expertise, and develop analytical tools and models to support our examination functions. For example, our Canary monitoring system monitors and identifies banks that may have high or increasing levels of credit, liquidity, or interest rate risks. Our credit risk and economics staffs have developed various analytical tools that assist examiners to identify portfolio or industry concentrations where risk may be increasing for more in-depth investigation. Our Risk Analysis unit – staffed by Ph.D. economists – provides on-site technical assistance to our resident staff in evaluating banks' quantitative risk models and measurement systems. Our National Risk Committee serves as a coordinating body to gather and disseminate information from throughout the OCC and the financial markets on emerging risk issues and advises me and the OCC's Executive Committee on quarterly basis of emerging issues and potential policy and supervisory responses.

Our combination of continuous on-site supervision, with the "ground level" intelligence it provides on each individual bank's activities and strategies, coupled with our broader, systemic risk analyses, allows us quickly to adjust our supervisory strategies to emerging risks and issues that may arise at individual institutions, within business segments or across the industry as a

whole. It also allows us to leverage the diverse skill sets that are needed to supervise our most complex institutions effectively.

Regulatory Coordination

We also work closely with other Federal regulators in carrying out our supervisory responsibilities through a variety of formal and informal mechanisms. Primarily through the Federal Financial Institutions Examination Council (FFIEC), the OCC works with the other Federal financial regulators (Board of Governors of the Federal Reserve System, FDIC, Office of Thrift Supervision, and National Credit Union Administration) to coordinate supervisory policies, regulations and regulatory reporting requirements, and examiner training on issues that cut across the banking system. Indeed, such coordination is the norm, not the exception among the Federal banking agencies. This coordination reduces regulatory burden by promoting greater uniformity, consistency, and efficiency in the supervision of insured depository institutions.

For example, during the past year the OCC worked together with the other Federal banking agencies on a variety of policy initiatives in areas such as bank technology, identity theft and consumer privacy and disclosure issues, and implementation of the USA PATRIOT Act.

In the area of bank technology, the banking agencies are undertaking a complete revision and update of the 1996 FFIEC Information Systems Examination handbook. A series of twelve, topical booklets addressing issues such as business continuity planning, information security, outsourcing (including off-shore outsourcing), and electronic banking will replace the 1996 handbook. The OCC also continues to coordinate with the Treasury Department's Financial and Banking Information Infrastructure Committee (FBIIC) and other agencies on issues related to improving the reliability and security of the U.S. financial system. These efforts have included sponsoring critical financial institutions' access to the Telecommunications Service Priority Program that provides priority treatment for the restoration or provisioning of telecommunications services in emergencies, and joint publication by the OCC, FRB and SEC, of an Interagency Paper on Sound Practices to Strengthen the Resilience of the U.S. Financial System. The paper identifies sound practices and steps necessary to protect the U.S. financial systems from the systemic effects of a wide-scale disruption.

We also are working closely with other regulators in the important areas of identity theft and consumer privacy. Last August, we and the other Federal banking agencies issued for comment proposed guidance that would require financial institutions to develop programs to respond to incidents of unauthorized access to customer information, including procedures for notifying customers under certain circumstances. The proposed guidance interprets the agencies' customer information security guidelines that require financial institutions to implement information security programs designed to protect their customers' information. We also are working closely with the Federal Reserve, the Federal Trade Commission and other agencies on implementation of the various provisions of the FACT Act.

Recognizing the importance of informing consumers about financial institutions' privacy policies and how consumers may affect information-sharing practices, the OCC, the other Federal banking agencies and the FTC issued in December, 2003, an advance notice of proposed

rulemaking to seek public comment on how to simplify privacy notices required under GLBA. With the other regulators, we have been meeting with consumer groups, as well as the Internal Revenue Service and Food and Drug Administration to get insights on how the banking agencies could use consumer testing to enhance the effectiveness of privacy notices.

To help alert consumers to potential pitfalls associated with certain high-cost mortgage and home equity loans, the agencies in conjunction with the Department of Housing and Urban Development, the Department of Justice, the Federal Housing Finance Board, the Federal Trade Commission, the National Credit Union Administration, and the Office of Federal Housing Enterprise Oversight, issued in October, 2003, a consumer brochure on predatory lending. The brochure, *Putting Your Home on the Loan Line is Risky Business,* cautions consumers about various predatory lending practices and advises consumers on steps they can take to protect themselves against such practices.

The OCC also works closely with law enforcement, the Treasury Department, and other Federal agencies, to disseminate information and take appropriate actions to help facilitate the prevention, detection, and prosecution of international money laundering and terrorist financing. For example, in May 2003, the FFIEC agencies, in cooperation with Treasury, the SEC and the CFTC, issued implementing regulations for the Customer Identification Program requirements of Section 326 of the USA PATRIOT Act. These and other USA PATRIOT Act requirements will be subject to examination reviews conducted in accordance with standards coordinated among the FFIEC agencies.

In addition to coordinating efforts on broad policy issues, we work closely with other regulators in our on-going bank examination programs. To the extent possible, we and the other banking agencies build upon each other's supervisory reviews and databases to minimize regulatory burden. We routinely share reports of examination, inspection reports, and other agency-institution communications and provide each other with access to our organizations' structure, financial, and supervisory information. To help facilitate and coordinate our supervision of large, complex institutions, we share information on proposed examination and supervisory activities for the coming year and coordinate the planning and execution of those activities in such a way as to minimize or eliminate any overlap or duplication. When appropriate, we hold joint meetings with institutions involving matters of mutual interest and may conduct coordinated reviews or examinations where a business activity is conducted across legal entities. For example, the OCC worked closely with the Federal Reserve throughout 2003 to investigate and respond to questions about potential illegal tying activities at large, insured depository institutions. Similarly, the Federal Reserve, the OCC, and the SEC worked together closely throughout 2002 and 2003 to examine and respond to questions relating to structured finance transactions of the Enron Corporation. The OCC participates annually on an interagency basis in the Shared National Credit Program established to provide a periodic credit risk assessment of supervised institutions' largest and most complex credit facilities.

Our information sharing and coordination efforts extend beyond the other Federal banking agencies and include State insurance departments and foreign bank regulators. For example, consistent with GLBA, the OCC has entered into information-sharing agreements with 49 State insurance departments and we meet regularly with the National Association of Insurance

Commissioners to discuss topics of mutual interest. We have also entered into 11 information-sharing agreements with foreign bank regulators to promote more efficient supervision of institutions with foreign operations.[3]

Basel II Developments

Because national banks have international as well as domestic operations, the OCC must – and we do – become involved in the development of approaches to bank supervision at the international level. Currently, the most significant of these approaches is the ongoing effort to revise the 1988 Basel Capital Accord. Let me briefly provide you a status report on this effort.

There have been a number of articles in the press in recent weeks about positions that U.S. regulators, and the OCC in particular, may be taking that I believe warrant some clarification and amplification.

First, let me stress that my U.S. colleagues and I share the overarching goal that Chairman Oxley expressed in his opening statement at this Committee's March 4, 2003 Oversight Hearing: that Basel II be implemented in a manner that is entirely consistent with the safety and soundness and continued competitive strength of the U.S. banking system.

As I have said, banks' current financial and capital positions are strong, but as the industry continues to evolve, so does its risk profile. Recognizing and adapting to changing risk profiles and changing risk management practices is critical to maintaining those strengths. These observations inform our approach to negotiations in the Basel Committee on Banking Supervision regarding Basel II. However, while we recognize that we can and should improve capital regulation to take into account changes in banking and risk management, a basic tenet in our negotiations over reform of the international capital standards is to *do no harm*. U.S. banks are world leaders in many aspects of banking – credit cards and securitizations, for example – and we must assure that these important markets are not disrupted or impaired in the name of achieving international conformity in capital rules. In view of the fundamental strength and resilience of the U.S. financial system, we believe that reforms to our regulatory and supervisory structure must be adopted in a prudent, reflective fashion.

Thus we are fully committed to three things: first, an open rule making process in which comments are invited and considered, good suggestions are heeded, and legitimate concerns are addressed; second, a reliable quantitative analysis in which we can assess the likely impact of Basel II on the capital of our banks <u>prior</u> to its adoption; and third, a prudent implementation in which we make well reasoned and well understood changes to bank capital requirements and incorporate in those changes appropriate conservatism. In this regard, I welcome the questions and issues that members of this Committee and its staff have raised about this important project

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[3] The U.S. Federal banking supervisors have concluded memoranda of understanding or statements of cooperation with supervisors in the following jurisdictions: the European Union, Argentina, Brazil, Canada, Chile, Germany, Hong Kong, Mexico, the Netherlands, Panama, and the United Kingdom. A number of others are in process. The OCC also has entered into some less formal information sharing arrangements with several other countries, including the Republic of China.

and I have repeatedly stressed to the Basel Committee the important role that Congressional oversight plays in our deliberative process.

The U.S. agencies' insistence on a thorough and rigorous deliberative process already has resulted in important modifications to the Basel II proposals. One of the most significant of these issues – and one that U.S. banks were virtually unanimous in criticizing in response to the Basel Committee's third consultative paper (CP-3) – involved the fundamental question of what losses capital requirements should be designed to cover. CP-3 would have calibrated capital to ensure coverage of both expected losses (EL) plus unexpected losses (UL). However, banks in the U.S. today generally measure and manage their internal economic capital allocations by reference to UL only, and most banks consider EL to be covered by a combination of reserves and credit pricing. As we examined this issue, we became convinced not only that the banks were conceptually correct in their arguments, but that retaining the EL plus UL calibration would have severe ramifications – not the least of which might be to seriously jeopardize the industry's acceptance of Basel II framework as being a conceptually sound framework. While many on the Basel Committee resisted this initially, the Committee ultimately put forth a new proposal in October to modify the calibration of Basel II to UL only. This modification was strongly endorsed by industry participants and has now been agreed to by the Committee.

The Committee announced several other important modifications to CP-3 in January that are responsive to numerous comments we received on CP-3 and the U.S. agencies' advanced notice of proposed rulemaking (ANPR) that was issued last August. These modifications include simplifying the proposed treatment for securitizations and aligning it more closely to industry practice and an agreement to find a prudentially sound solution that better recognizes credit mitigation techniques used by the industry. Other issues are still under discussion by the Committee's various technical working groups and are scheduled to be considered by the Committee at its meeting in May.

Probably the most difficult policy issue remaining involves the appropriate risk-based capital treatment of certain retail credit products – unused credit card lines in particular. This issue is critically important for national banks and for the cost and availability of consumer credit. It is also an area in which consensus has been hard to come by, not least because of the extent to which American credit card products are marketed and administered differently than in other parts of the world. Given the prominence of this issue for U.S. banks, and for national banks in particular, there is little room for substantive compromise, and the OCC will not accept provisions that are likely to unduly disrupt or disadvantage established, well-functioning business practices for the sake of global conformity.

Notwithstanding the difficulty of these issues, the Committee's goal is to be in a position by mid-year to release a text that will provide the basis for each country's national implementation process. Let me reiterate that point: the release of the next round of Basel II proposal does not represent a final agreement or accord; rather, it is the platform from which we will launch our more in-depth domestic deliberative process. In the U.S., that process will have several key steps.

First, the U.S. agencies will conduct a fourth quantitative impact study (QIS 4) in the third and fourth quarters of this year. This study will be based on the Committee's mid-year release and will differ in some important aspects from the Basel Committee's earlier quantitative studies. QIS-4 will not only be conducted against the background of a more fully articulated proposal, but will include a more prominent supervisory role to ensure greater reliability and consistency in survey results than has occurred in the past. We continue to believe that we cannot responsibly adopt final rules implementing Basel II until we have both determined with a high degree of reliability what the impact will be on the capital of our banks, and we have made the judgment that the impact is acceptable and conducive to the maintenance of a safe and sound banking system in the U.S. We believe the results of QIS 4 will be more useful than any data we currently have in determining the magnitude of Basel II on bank capital and potential competitive inequities, as well as determining ultimately what to do about them.

Second, in another effort to increase our practical understanding of the effects of Basel, the U.S. agencies have commenced an operational risk benchmarking review at a number of institutions. Information obtained through this effort will enhance agency understanding of current qualitative and quantitative operational risk practices and will assist agency efforts to develop additional supervisory guidance and training materials for banks and examiners on the operational risk component of Basel II. Throughout this period we will continue our dialogue with banks and other interested stakeholders on various issues that Basel II may raise.

These projects and discussions will help us in the third key step in Basel implementation, developing a joint notice of proposed rulemaking (NPR) that will set forth the proposed regulatory text for Basel II in the U.S. Currently we anticipate that such an NPR will be released for public comment in late 2005 or early 2006. At the OCC, we have made a preliminary determination that this rulemaking will be a "significant regulatory action" for purposes of Executive Order 12866. Consequently, we will prepare and submit to the Office of Management and Budget's (OMB) Office of Information and Regulatory Affairs (OIRA) an economic analysis that includes:

- a description of the need for the rules and an explanation of how they will meet the need;
- an assessment of the benefits anticipated from the rules together with, to the extent feasible, a quantification of those benefits;
- an assessment of the costs anticipated from the rules together with, to the extent feasible, a quantification of those costs; and
- an assessment of potentially effective and reasonably feasible alternatives to the planned regulation and an explanation why the planned regulatory action is preferable to the identified potential alternatives.

We have begun discussions with the OMB's OIRA regarding the how these analyses will be designed and conducted. Our analysis will be published as part of our notice and comment process.

Finally, as the rulemaking process for the domestic implementation of Basel II moves forward, we and the other U.S. agencies are exploring the implications that Basel II may have on non-

mandatory banks and what, if any changes we should make to our capital regulations for those banks. Any such changes will, of course, be subject to public notice and comment.

As my testimony conveys, while we have made important strides in trying to develop a more risk-sensitive capital framework for internationally active banks, there is still a long way to go before Basel II is completed and adopted. As I have repeatedly stated before Congress and in the Basel Committee, a new accord cannot be completely finalized until national implementation procedures have been completed and I am committed to a notice and comment process that is open and fair and responsive to public comments. The OCC and other U.S. agencies have recognized the possibility that, even in the late stages, public comments might reveal flaws in the proposal that will need to be addressed before we can issue final implementing regulations. The OCC's ultimate willingness to sign onto Basel II is going to depend on whether we are satisfied with the final product.

The Applicability of State Law to National Banks

National banks today compete in a financial services marketplace that is profoundly different from the one they confronted 20, even 10, years ago. Legal barriers to banks' geographic expansion have been eroded by market developments and, in some cases, eliminated by Congress. At the same time, technology has enabled ways of doing business that have vastly expanded their markets. Consumers can comparison shop for financial products and services on-line and can initiate financial transactions over the Internet. Banks use technology to make available a wider array of products and services and to deliver those products and services more quickly. Credit decisions – like approving a mortgage loan – that used to take weeks can now be made in a matter of hours, for a customer located across the desk or across the country. In our highly mobile society, consumers expect that, when they move, they can take with them the financial relationships they have worked to establish with their banks. All these factors have combined to produce a market for credit, deposits, and many other financial products and services that is now national, and for some banks, international, in scope. In other words, through advances in data analysis and communications and changes in customer demographics, banking markets have expanded beyond the locality in which a given customer may be resident.

These developments highlight the significance of being able to conduct a banking business pursuant to consistent, national standards, regardless of the location of a customer when he or she first becomes a bank customer or the location to which the customer may move *after* becoming a bank customer. Yet the trend at the State – and sometimes the local – level has been the enactment of an increasingly diverse and potentially conflicting assortment of laws that localize bank regulation and threaten the ability of national banks to operate under the powers granted by their Federal charter, pursuant to uniform national standards, and subject to Federal oversight and supervision. In addition to conflicting with Federal authorities, these State and local laws have resulted in greater uncertainty about the standards applicable to national banks' operations, costly litigation to resolve that uncertainty, and in some respects, constriction of the availability of legitimate credit.

In January of this year, the OCC issued two final rules – our preemption rule and amendments to our existing visitorial powers rule – intended to provide national banks with the guidance they

need to operate under uniform, predictable Federal standards – plus rigorous standards of consumer protection. In the latter respect, our second and equally important goal was to ensure that the Federal standards under which national banks operate directly address and prevent abusive or predatory lending practices.

The preemption rule adds provisions to our regulations expressly addressing the applicability of certain types of State laws to national banks' lending and deposit-taking activities. The rule is not a dramatic expansion of preemption. The regulation only preempts the types of laws that are listed in the regulation. The listed types of laws are ones that already are preempted under longstanding, preexisting OCC regulations, have been found to be preempted in OCC preemption opinions, have been found to be preempted by the courts, or have been determined to be preempted for Federal thrifts by the OTS. Thus, they are types of laws for which substantial precedent exists recognizing the interference they pose to the ability of Federally-chartered institutions to operate under uniform Federal standards. We will continue to evaluate other types of laws, not listed in the regulations, under the pre-existing, judicially established standards for Federal preemption that are encapsulated by the "obstruct, impair, or condition" phrasing contained in the rule. It is important to stress that this phrase does not itself preempt any State law; rather it distills the standard that we believe the courts would apply in deciding questions of preemption for the types of laws not listed in the regulation.

Our second action involved amendments to our existing regulation concerning the OCC's exclusive "visitorial powers" with respect to national banks.[4] Existing, longstanding OCC regulations implement the visitorial powers statute by providing that State officials are not authorized to inspect, examine, or regulate national banks, except where another Federal law authorizes them to do so. One amendment to our visitorial powers rule clarified that the scope of the OCC's exclusive visitorial authority applies to the content and conduct of national bank activities authorized under Federal law. In other words, the OCC is exclusive supervisor of a national bank's banking activities. Another amendment clarifies that the *preservation* of visitorial powers "vested in the courts of justice" does not *grant* State regulatory or law enforcement officials *new* authority, in addition to whatever they may otherwise have, to exercise visitorial powers over national banks. State Attorneys General do not dispute that Federal law prohibits them from examining or taking actions directly against national banks, such as through cease and desist proceedings.[5] What we have said is simply that they may not use the courts to accomplish indirectly what they acknowledge Federal law clearly prohibits them from accomplishing directly.

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[4] "Visitorial powers" is a term used to refer to the authority to examine, supervise, and regulate the affairs of a corporate entity. Under Federal law, the OCC has exclusive visitorial powers over national banks – except where Federal law provides otherwise. Specifically, 12 U.S.C. § 484 provides that "no national bank shall be subject to any visitorial powers except as authorized by Federal law, vested in the courts of justice" or exercised by Congress or a committee of Congress. This provision, originally enacted in 1863, is integral to the overall design of the system and the ability of national banks to conduct the business of banking subject to uniform, consistent standards and supervision, wherever in the nation they operate.

[5] See Footnote 28 in Brief of Amici Curiae of 41 State Attorneys General in support of Defendant, in Wachovia Bank, N.A. v. Watters, Civil Action No. 5:03CV0105, U.S. District Court for the Western District of Michigan, January 29, 2004.

These rules were the subject of thorough examination by this Committee's Subcommittee on Oversight and Investigations at a hearing held earlier this year. The written statement we submitted for that hearing contains a comprehensive description of the rules, the legal principles that support them, and our reasons for adopting them, and I would refer the members of the Committee to that earlier statement for detailed discussion of those matters.[6]

Today, I want to correct the record on three points that have been the subject of a great deal of confusion, misunderstanding, and mischaracterization in recent weeks:

- The OCC's preemption and visitorial powers rules do not leave consumers vulnerable to predatory or abusive lending practices.

- The OCC employs a comprehensive, integrated approach to compliance supervision, staffed with resources ample to ensure that national bank consumers are protected.

- The OCC welcomes new opportunities to cooperate with State authorities on issues of mutual concern pertaining to consumer protection.

1. The OCC's rules do not leave consumers vulnerable to abusive lending practices.

It is simply not the case that national bank customers are left exposed to abusive practices as a result of our rules. First, national banks and their operating subsidiaries are not where predatory and abusive lending practices are festering. Second, national banks and their operating subsidiaries are governed by strong Federal standards designed to prevent these practices. Finally, the OCC has a strong track record of taking vigorous enforcement action to remedy any such practices that do occur and require restitution to customers.

Clearly, there is a real problem with abusive lending practices in this country, but national banks are not the breeding ground.[7] Whatever our differences of opinion with the State Attorneys

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[6] See "Testimony of Julie L. Williams, First Senior Deputy Comptroller and Chief Counsel, Office of the Comptroller of the Currency, Before the Subcommittee on Oversight and Investigations of the Committee on Financial Services of the U.S. House of Representatives," January 28, 2004 (Williams Testimony).

[7] This conclusion is borne out not only by our own supervisory experience, but also by an extensive study of predatory lending conducted by the Department of Housing and Urban Development (HUD) and the Treasury Department. A Treasury-HUD joint report issued in 2000 found that predatory lending practices in the subprime market are less likely to occur in lending by –

> banks, thrifts, and credit unions that are subject to extensive oversight and regulation . . . . The subprime mortgage and finance companies that dominate mortgage lending in many low-income and minority communities, while subject to the same consumer protection laws, are not subject to as much federal oversight as their prime market counterparts – who are largely federally-supervised banks, thrifts, and credit unions. The absence of such accountability may create an environment where predatory practices flourish because they are unlikely to be detected.

Departments of Housing and Urban Development and the Treasury, "Curbing Predatory Home Mortgage Lending: A Joint Report" 17-18 (June 2000), available at http://www.treas.gov/press/releases/report3076.htm.

General, they have stated unambiguously in various filings that there is scant evidence that national banks, or their operating subsidiaries, are engaged in abusive lending practices.[8] Indeed, these State officials have recognized the extent to which banks (and thrifts) are highly regulated and closely supervised, and have credited that regulatory presence for the scarcity of evidence of abusive or predatory practices.

Our preemption rule contains two new provisions that expressly prohibit abusive or predatory lending practices by national banks or their operating subsidiaries. First, the rule prohibits national banks from making any consumer loan based predominantly on the foreclosure or liquidation value of a borrower's collateral, rather than on the borrower's ability to repay the loan according to its terms. This anti-predatory lending standard applies uniformly to all consumer lending activities of national banks and their operating subsidiaries, regardless of the location from which those activities are conducted or where customers reside. This standard strikes at the heart of predatory lending, namely lending practices that effectively swindle a homeowner out of his or her property.[9]

Second, our preemption rule provides that, in connection with *any* type of lending, national banks and their operating subsidiaries shall not engage in unfair and deceptive practices within the meaning of Section 5 of the Federal Trade Commission Act (FTC Act), which prohibits "unfair or deceptive acts or practices" in interstate commerce. Although we do not have the statutory authority to define particular acts or practices as "unfair" or "deceptive" under the FTC Act, we added an express reference to Section 5 to our rule in response to commenters who urged us to affirm that the principles of the Act apply to national banks. We viewed this addition as particularly appropriate in light of the fact that the OCC pioneered the use of Section 5 as a basis for enforcement actions against banks that have engaged in such conduct, and have obtained substantial restitution for customers as a result.

These new standards are comprehensive and they apply nationwide, to all national banks and their operating subsidiaries. They apply strong protections for national bank customers in every State – including the many states that do not have their own anti-predatory lending standards.

The addition of these provisions to our lending rules reinforces the obligation of national banks and their operating subsidiaries to treat their customers fairly and operate pursuant to high standards of integrity. The provisions supplement prior OCC predatory lending guidance[10] and a

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In addition, the report found that a significant source of abusive lending practices is non-regulated mortgage brokers and similar intermediaries who, because they "do not actually take on the credit risk of making the loan, . . . may be less concerned about the loan's ultimate repayment, and more concerned with the fee income they earn from the transaction." Id. at 40.

[8] Brief for Amicus Curiae State Attorneys General, Nat'l Home Equity Mortgage Ass'n v. OTS, Civil Action No. 02-2506 (GK) (D.D.C.) at 10-11 (emphasis added). See also National Association of Attorneys General, Comment Letter Re: Docket No. 03-16 (dated Oct. 6, 2003) at 10.

[9] See also OCC Advisory Letter 2002-3, "Guidance on Unfair or Deceptive Acts or Practices," March 22, 2002.

[10] The OCC was the first Federal banking agency to issue anti-predatory lending guidance. Two advisory letters issued a year ago provide comprehensive supervisory guidance directed at ensuring that national banks and their operating subsidiaries do not become involved in abusive or predatory mortgage lending practices. See OCC

host of Federal consumer protection laws that apply to national banks and their operating subsidiaries.[11]

If, as a result of our examination or supervisory processes, or upon investigation of referrals or complaints, we find abusive practices in a particular institution, our track record compellingly shows that we take action to stop them. Section 8 of the Federal Deposit Insurance Act gives the OCC broad powers to require compliance with any "law, rule, or regulation." This includes the ability to issue cease and desist orders when the OCC determines that a national bank or its operating subsidiary has violated any applicable Federal law or regulation or any applicable State law or regulation.[12] In an appropriate case, the cease and desist order may include restitution or a requirement for such other affirmative action as the OCC determines is appropriate.[13] Our record shows that we have been willing and able to use these remedies to protect customers and to address unfair, deceptive, or abusive practices when such situations occur.[14]

2. ***The OCC has ample resources to ensure that national bank customers are protected.***

Advisory Letter 2003-2, "Guidelines for National Banks to Guard Against Predatory and Abusive Lending Practices," February 18, 2003; OCC Advisory Letter 2003-3, "Avoiding Predatory and Abusive Lending Practices in Brokered and Purchased Loans," February 18, 2003.

[11] Federal consumer protection laws and regulations that apply to national banks and to national bank operating subsidiaries include: the Federal Trade Commission Act; Truth in Lending Act; Home Ownership and Equity Protection Act; Fair Housing Act; Equal Credit Opportunity Act; Real Estate Settlement Procedures Act; Community Reinvestment Act; Truth in Savings Act; Electronic Fund Transfer Act; Expedited Funds Availability Act; Flood Disaster Protection Act; Home Mortgage Disclosure Act; Fair Housing Home Loan Data System; Credit Practices Rule; Fair Credit Reporting Act; Federal Privacy Laws; Fair Debt Collection Practices Act; the new OCC anti-predatory lending rules in 12 C.F.R. Parts 7 and 34; OCC rules imposing consumer protections in connection with the sales of debt cancellation and suspension agreements; OCC standards on unfair and deceptive practices http://www.occ.treas.gov/ftp/advisory/2002-3.doc.); and OCC standards on preventing predatory and abusive practices in direct lending and brokered and purchased loan transactions (http://www.occ.treas.gov/ftp/advisory/2003-2.doc. and http://www.occ.treas.gov/ftp/advisory/2003-3.doc.).

[12] 12 U.S.C. § 1818(b)(1). See National State Bank of Elizabeth, N.J. v. Long, 630 F.2d 981, 988-89 (3d Cir. 1980) (confirming the OCC's authority under 12 U.S.C. § 484 to enforce an applicable State redlining statute).

[13] 12 U.S.C. § 1818(b)(6).

[14] See the following actions taken by the OCC under the FTC Act to address unfair or deceptive practices: In the Matter of Clear Lake National Bank, San Antonio, Texas, Enforcement Action 2003-135 (required restitution of fees and interest for home equity loans); In the Matter of First Consumers National Bank, Beaverton, Oregon, Enforcement Action 2003-100 (required restitution of annual fees and overlimit fees for credit cards); In the Matter of Household Bank (SB), N.A., Las Vegas, Nevada, Enforcement Action 2003-17 (required restitution regarding private label credit cards); In the Matter of First National Bank in Brookings, Brookings, South Dakota, Enforcement Action 2003-1 (required restitution regarding credit cards); In the Matter of First National Bank of Marin, Las Vegas, Nevada, Enforcement Action 2001-97 (restitution regarding credit cards); and In the Matter of Direct Merchants Credit Card Bank, N.A., Scottsdale, Arizona, Enforcement Action 2001-24 (restitution regarding credit cards). See also the following actions taken by the OCC regarding payday lending activities of national banks: In the Matter of Peoples National Bank, Paris, Texas, Enforcement Action 2003-2; In the Matter of First National Bank in Brookings, Brookings, South Dakota, Enforcement Action 2003-1; In the Matter of Goleta National Bank, Goleta, California, Enforcement Action 2002-93; and In the Matter of Eagle National Bank, Upper Darby, Pennsylvania, Enforcement Action 2001-104. These orders can be found on the OCC's website within the "Popular FOIA Requests" section at http://www.occ.treas.gov/foia/foiadocs.htm.

The central feature of the OCC's consumer compliance supervision is our on-site presence in the institutions we supervise. National banks and national bank operating subsidiaries are subject to comprehensive, regular – in the case of large banks, continuous – program of supervision that is, as I have described, risk-focused and rigorous.

Federal law requires that the OCC examine national banks at least once every 12 or 18 months, depending on the size of the bank.[15] However, the largest national banks have on-site examination teams conducting continuous examinations of all aspects of the bank's operations. In addition, the OCC may at any time conduct targeted safety and soundness and compliance examinations.

Our system of supervision applies to national banks and their operating subsidiaries. The OCC supervises national banks by business line, not according to corporate form, so the standards applied in the course of that supervision are the same for national banks and their operating subsidiaries. The book figures of a parent national bank and its operating subsidiaries are combined for purposes of applying statutory or regulatory limits, such as lending limits or dividend restrictions. The OCC reviews the institution's policies and procedures in an effort to assess whether they adequately identify and address the risks the institution may face, given the nature and scope of its business. Finally, the OCC evaluates the adequacy of all elements of the institution's business, including capital, earnings, assets, management, liquidity, sensitivity to market risk, and information systems.

Through our safety and soundness and compliance examinations, the OCC reviews the adequacy of the bank's policies, systems and controls, relative to the character and complexity of the bank's business and assesses whether the bank's activities are being carried out in compliance with applicable laws and regulations. As part of these reviews, examiners typically sample transactions to assess the adequacy of the bank's systems and controls. For example, as part of an asset quality review, the sample of loans will be reviewed to determine the quality of the loans, the adequacy and completeness of the information concerning the loan and the borrower, and whether the lending function is being carried out in compliance with applicable laws.

Depending on the bank's risk profile and other supervisory information, examiners may target their reviews to a particular loan product, business line, or operating unit. For example, if the bank is engaging in significant new or expanded mortgage lending activities through an operating subsidiary, examiners normally would select a sample of those loans for review. Similarly, as part of our compliance reviews, examiners may select a sample of consumer loan or deposit products to verify that the bank's systems and controls are adequate and that the bank is complying with applicable consumer protection laws and regulations. If the sampling process indicates potential issues, we will expand our reviews. The examination process is intended to provide a high level of assurance that each aspect of an institution's business is conducted in compliance with applicable laws and on a safe and sound basis. Through this process, we are

[15] 12 U.S.C. § 1820(d)(1). The general rule requires examinations every 12 months. However, if a bank has less than $250 million in assets and is in good condition, the OCC need only examine it at least once every 18 months. Id. § 1820(d)(4).

able to examine national banks and their operating subsidiaries for potentially abusive lending practices as well as compliance with the host of specific Federal consumer protection requirements to which they are subject. Our compliance supervision is an integral part of our comprehensive, ongoing oversight of the national banking system.

Today, the OCC supervises approximately 2100 national banks, together with their operating subsidiaries. Compliance and enforcement at the OCC are carried out through our corps of bank examiners and attorneys. We have nearly 1700 examiners in the field, hundreds of whom are involved in both safety and soundness and compliance supervision. Over 100 examiners throughout the country work exclusively on compliance supervision. We have over 300 examiners on site at our largest national banks, engaged in continuous supervision of all aspects of their operations. These resources are supplemented by dozens of attorneys in our district offices and Washington D.C. who work on compliance matters.

The employees in our Customer Assistance Group (CAG) located in Houston, Texas, further supplement these functions. The CAG provides direct assistance to customers of national banks and their subsidiaries to resolve individual complaints. It also collates and disseminates complaint data that help point our examiners toward banks, activities, and products that require further investigation or transaction testing through product sampling. While the CAG is an important supplement to our compliance supervision functions, it is by no means all there is to it.

It is important to note, by way of comparison, based on data published by the Conference of State Bank Supervisors, State banking departments collectively supervise approximately 113,000 entities, of which approximately 6,000 are commercial banks.[16] For all these entities, the States report that they have 2,308 examiners.[17] Thus, if one were to look only at commercial banks and assume all State examiners were dedicated to commercial bank supervision, OCC's resources exceed those of the States on a per-supervised bank basis. But, in fact, State banking departments are responsible for many entities in addition to commercial banks. These include, depending on the State, savings banks, thrifts, credit unions, bank holding companies, mortgage bankers and brokers, industrial loan companies, non-bank trust companies, money transmitters, consumer finance companies, other licensed lenders, payday lenders, title lenders, check cashers, pawnshops, bankers' banks, securities brokers and dealers, and funeral parlors. Thus, on a per-supervised entity basis, the OCC has significantly more resources than do the States.[18] This is exactly the opposite of what some critics of our regulations have suggested. These suggestions – that our resources are inadequate to enable the OCC to supervise compliance effectively or to fulfill the consumer protection aspect of our mission – are simply without foundation.

3. The OCC welcomes opportunities to cooperate with States on issues pertaining to consumer protection.

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[16] A Profile of State Chartered Banking, Nineteenth Edition, 2002-2003, Conference of State Bank Supervisors.

[17] Id.

[18] See attached chart.

The OCC and the States have a long history of coordination and cooperation, which we wish to continue. Neither the preemption rule nor the revised visitorial powers rule results in the OCC taking over a vast domain of supervisory and enforcement activity currently being conducted by State authorities with respect to national banks. The rules do not effect the ability of States to engage in those activities, where authorized by Federal law, e.g., securities, insurance, telemarketing, nor do the rules prevent State officials from applying and enforcing generally applicable State laws that do not attempt to control the content or conduct of national banks' banking activities. Our jurisdiction over national banks and their subsidiaries does not deprive State regulators of a role in protecting consumers in their States. We welcome the opportunity to work cooperatively with them to further that goal. We have invited State authorities to refer consumer complaints concerning national banks to the OCC, and to bring to our attention concerns that any national bank is engaged in unfair, deceptive, abusive or predatory practices. We have set up special procedures to handle and track referrals from State authorities. Unfortunately, we have received very little response to the overtures.

The OCC and the states already cooperate extensively in many respects, referring consumer complaints to the appropriate regulator of the entity generating the complaint, and we welcome additional opportunities to collaborate. Recently, the OCC issued a new advisory letter to national banks clarifying our expectations about how they should handle customer complaints that are forwarded to them from State agencies and departments.[19] We took that opportunity to emphasize the importance of resolving consumer complaints fairly and expeditiously, regardless of the source of the complaint, and to remind banks that their complaint resolution processes are subject to review as part of our regular supervision of their compliance management programs.

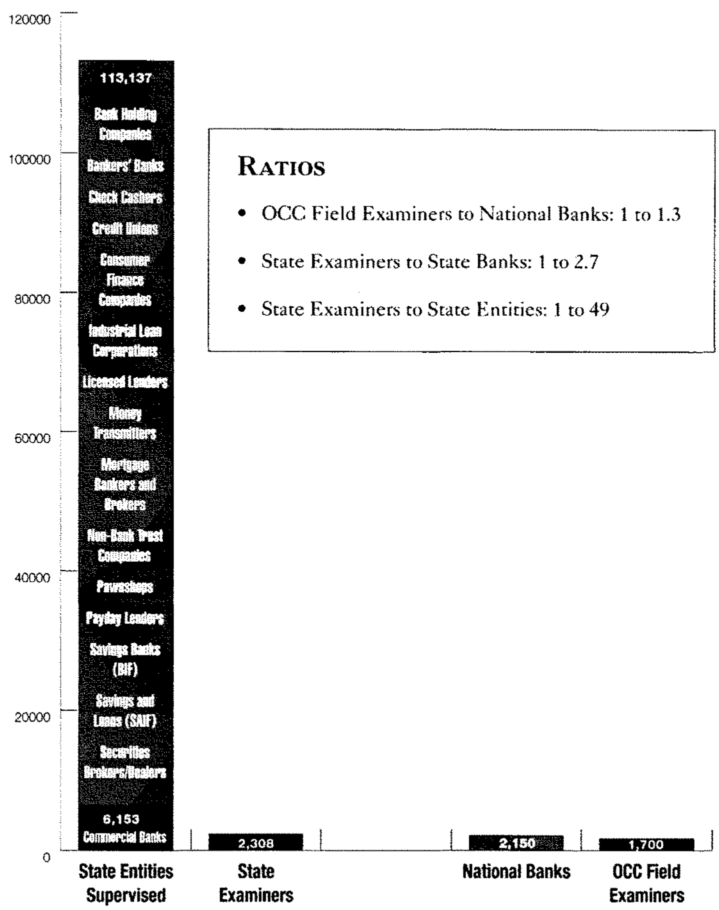
There may ultimately be some areas where we will have to agree to disagree, but I am confident that there are many more where we can agree that there are improvements that all of us can make in how consumer concerns are identified and resolved. We welcome the opportunity to have further dialogue to achieve those goals.

V. CONCLUSION

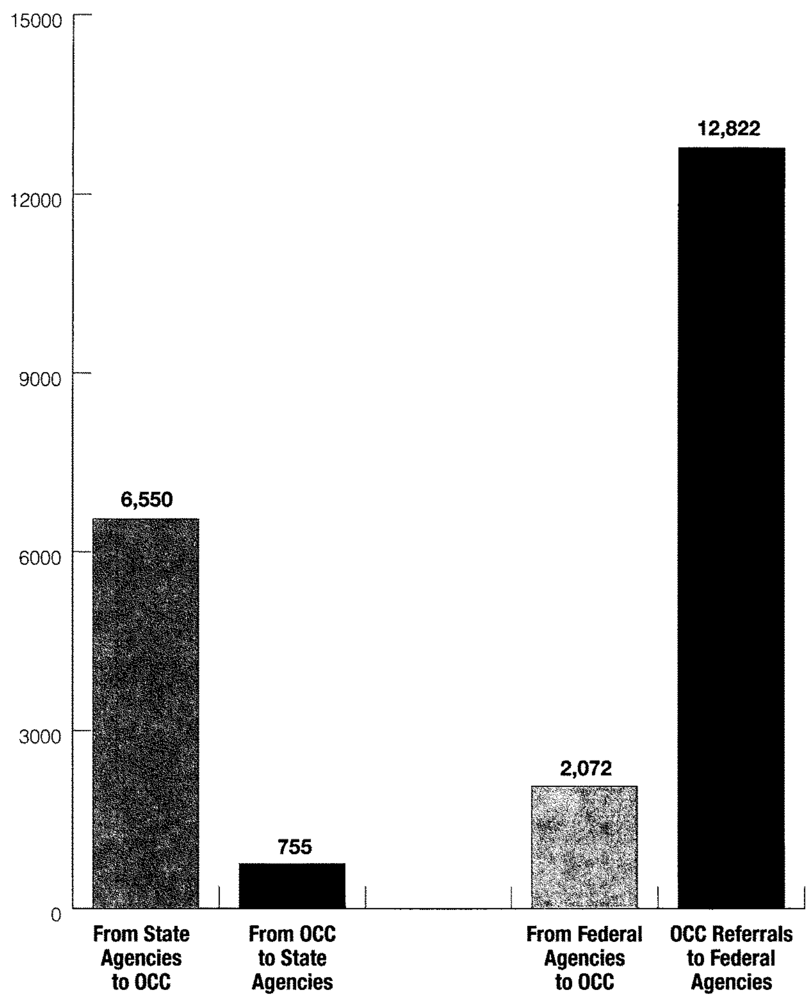
In conclusion, Mr. Chairman, the national banking system is sound, and its recent performance has been strong. It has successfully weathered the recent recession, and it is responding in dynamic fashion to the changes in the financial services marketplace. The OCC, too, is keenly focused on keeping pace with change – by refining our own management practices, by improving the approaches we use to supervise the industry, and by striving to ensure that national banks remain the safe, and sound, competitive, and high integrity engines of our economy that they were designed to be. We look forward to working productively with you, with the members of this Committee, and with State officials as we pursue our efforts to achieve that goal.

[19] OCC Advisory Letter 2004-2, "Consumer Complaints Referred to National Banks from State Officials," February 26, 2004.

Comparison of OCC and State Examiner Resources



2003 Referrals of Consumer Complaints



Article 1

THE WALL STREET JOURNAL.

Friendly Watchdog: Federal Regulator Often Helps Banks Fighting Consumers --- Dependent on Lenders' Fees, OCC Takes Their Side Against Local, State Laws --- Defending Uniform Rules

By Jess Bravin and Paul Beckett
Staff Reporters of The Wall Street Journal
2,849 words
28 January 2002
The Wall Street Journal
A1
English

When a federal appeals court in San Francisco took up the issue of automated-teller-machine fees earlier this month, it sparked the latest round in the battle between big banks and customers.

Sticking up for consumers were the cities of San Francisco and Santa Monica. They had banned certain ATM fees, after customers complained about being gouged when they use ATMs belonging to banks other than their own. Defending the fees were California's two largest banks -- Bank of America Corp. and Wells Fargo & Co. -- which had won at trial.

Also in the courtroom: the Office of the Comptroller of the Currency, the federal banking regulator. But in this case -- as in more than a dozen others in recent years -- the OCC wasn't there to check the economic power of banking titans. Instead, the regulator was helping the nationally chartered banks defend their fees. The appeals court is expected to rule in coming months.

Many federal regulators have a clear mandate to put consumers first. The Securities and Exchange Commission, for example, refers to itself as "the investor's advocate."

It's less clearcut for the federal banking watchdog. Time and again, the U.S. agency that bank customers might assume is on their side has lined up with banks to fight state and local measures that purport to aid consumers.

In addition to the ATM-fees case in California, the OCC recently has supported banks in their effort to kill a ban in Texas on certain check-cashing fees. In Pennsylvania and Rhode Island, the OCC has weighed in on the side of giant FleetBoston Financial Corp. against consumer allegations of improper increases in credit-card rates. And in Michigan, the federal agency has even supported a push by banks making auto loans to curb a state law aimed at unscrupulous car dealers.

The OCC's solicitousness toward the businesses it oversees stems in part from its need to compete for their loyalty. In an uncommon arrangement, banks can choose either a state or federal regulator, and the selection has financial consequences: The OCC and state banking departments subsist entirely on fees paid by the institutions they regulate.

The competition, though discreet, can get intense. As consolidation has swept the industry, the OCC's once-mighty position has slipped. Since 1990, as the number of U.S. banks dropped 31%, to 8,300, the number regulated by the OCC dropped 45%, to about 2,230. It still regulates the bulk of the banking industry as measured by assets, but consolidation has made the agency increasingly dependent on a few big players. Third-ranking Bank of America, based in Charlotte, N.C., now pays $40 million a year to the OCC in fees, or the equivalent of 10% of the agency's annual $400 million budget.

The OCC promises federally chartered banks the predictability of a uniform set of rules, rather than the burden of complying with varying state standards. A further attraction is the likelihood that the agency will support its banks in court against aggressive state regulators. State banking authorities typically offer the competing enticement of lower examination fees.

The OCC, an arm of the Treasury Department with 2,900 employees, maintains that it safeguards customers by

enforcing federal consumer-protection laws and by securing the overall health of the national banking system. But the agency's chief, John D. Hawke Jr., says that state efforts to stick up for bank customers often threaten to undermine the right of national banks under federal law to operate and charge fees as they see fit.

The OCC's siding with banks in court fights "may operate in some cases to the disadvantage of consumers," says Mr. Hawke, a 68-year-old lawyer who in private practice represented both state- and federally chartered banks. But his agency "can't pick and choose whether a [state] law or action is good or bad" for consumers. If it cramps banks' freedom to operate in the eyes of the OCC, it must go, he says.

History helps explain the OCC's stance. It was founded during the Civil War to oversee newly created national banks that were formed to circulate a national currency and finance the Union's military campaign. With strong backing from the federal courts, the OCC still interprets the National Bank Act of 1863 as authorizing it to oppose any state or municipal attempt to interfere with the ability of nationally chartered banks to engage in "the business of banking." When the agency goes to court, it also invokes a provision in the U.S. Constitution stating that federal law prevails in conflicts with state law.

Frustrated consumers say the upshot is that the OCC favors the industry that pays its bills. "The individual bank customer is just no equal of the large banking institutions," says David Buda, an attorney in Fort Lee, N.J., who has complained unsuccessfully to the OCC about increases in the interest rate on his FleetBoston credit card. If "your only avenue is to complain to the comptroller of the currency, then all you're going to get is a form letter saying, `We can't help you,' " Mr. Buda adds.

Other federal regulators operate differently. The SEC budget comes from fees from securities exchanges and publicly traded companies. But unlike banks, those companies don't have a choice of regulator, so the SEC isn't competing for their loyalty. About 12% of the Food and Drug Administration's budget comes from industry fees. The Federal Trade Commission is funded by taxpayers.

During tough economic times, the bank-regulatory setup comes under a brighter spotlight. Consumers find it harder to keep up financially. Banks, faced with rising loan losses, seek additional revenue with moves such as fee hikes on credit cards -- making it that much more likely that consumers will seek help from the federal bank regulator.

Mr. Hawke, who was appointed by President Clinton in 1998 to a five-year term, says he spends time both looking out for consumers and seeking to defend his regulatory turf. In 1999, he introduced a 12-minute video the OCC distributes to banks called "The Value of the National Bank Charter." In it, he describes "how the OCC and a national charter can help banking organizations achieve their goals."

Sometimes, he makes personal appeals. In August 1999, when state-chartered AmSouth Bancorp of Birmingham, Ala., was in the process of buying OCC-chartered First American Corp. of Nashville, Tenn., Mr. Hawke flew to visit C. Dowd Ritter, AmSouth's chief executive. After exchanging pleasantries, Mr. Hawke reached into his briefcase to show Mr. Ritter a copy of a federal bank charter issued in 1884 to one of AmSouth's predecessor banks.

"This is something I thought you would like to see," Mr. Hawke said, according to Stephen Yoder, AmSouth's general counsel, who attended the meeting. "We have something in Washington that is part of your history."

Despite the imaginative appeal, AmSouth rebuffed Mr. Hawke, retaining its Alabama state charter after the merger. The bank says it already had a good relationship with its state regulator.

Mr. Hawke, who confirms the account, says that losing market share "is a matter of concern to us." But he stresses the OCC takes seriously its responsibility to protect consumers. He occasionally makes speeches chastising bankers for such practices as selling confidential customer information to telemarketing firms. And the agency enforces about a dozen federal consumer laws, including the Truth in Lending and Fair Credit Reporting Acts. Typically, the OCC enforces compliance with those laws during its routine bank examinations, agency spokesman Robert Garsson says.

Earlier this month, as the result of an examination, the OCC ordered Eagle National Bank, a small institution in Upper Darby, Pa., to get out of the business of funding so-called payday loans. These are high-interest loans repayable on the borrower's next payday and viewed by many regulators as exploitative. The OCC said it acted because Eagle's lack of oversight of the loans had placed its financial viability at risk.

In a separate case 18 months ago, the agency joined a civil probe initiated by the San Francisco district attorney into allegations that Providian Financial Corp., a San Francisco credit-card issuer, had misled customers about

interest rates on credit cards. Providian allegedly promised card holders they wouldn't have to pay an annual fee when the company in fact imposed a mandatory $156 annual charge for "credit protection." Without admitting wrongdoing, Providian agreed to pay $300 million to purported victims, plus a $5.5 million penalty to San Francisco. Mr. Hawke calls the case a landmark exercise of the OCC's authority to ban deceptive practices.

Still, he doesn't apologize for using the OCC's power to override state and local laws designed to protect consumers. Enjoying this aid provides an incentive for banks to sign up with the OCC, he says. "It is one of the advantages of a national charter, and I'm not the least bit ashamed to promote it." His counterparts at the SEC, FTC or FDA don't have a comparable turf-related incentive to advertise their ability to knock down state and local consumer-protection laws.

State banking regulators often engage in their own efforts to lure banks. The Kansas banking commissioner, for instance, promises on his official Web site that state-chartered banks will have greater ability "to lobby [the] state legislature for changes in laws and regulations." Commissioner Franklin Nelson explains in an interview that his department is next door to the statehouse and can help bank officials and their lobbyists reach lawmakers. The OCC can't offer such access, he says.

State regulators also aren't shy about pointing out that national banks pay as much as 2.5 times the annual examination fees charged to state banks. The fees are determined by bank size. A small bank, with $500 million in assets, would typically have to pay $43,000 under a state charter, compared with $113,000 under a federal charter, according to OCC estimates.

It is the OCC's ability to help override state laws that has the biggest impact on consumers. The OCC's involvement in the California ATM case began in 1999, when Bank of America and Wells Fargo, which together control more than 60% of the ATMs in the state, asked a federal judge in San Francisco to void that city's and Santa Monica's bans on some fees, which generate about $6 million annually for the two banks. The OCC, in separate legal papers, said "the public interest" favored allowing banks to charge noncustomers more for using their ATMs. Otherwise, the OCC argued, the banks would lack the incentive to operate large numbers of ATMs in areas where they don't have many customers.

"That's flat-out wrong," Santa Monica Mayor Michael Feinstein responds in an interview. "We are closer to that consumer than the OCC is," he adds. And, on balance, he says, consumers want lower fees, even in the face of bank threats to deny noncustomers any access to their ATMs.

Mr. Hawke suggests that angry customers do as he says he does: walk a few extra blocks to find a no-fee ATM.

A federal judge in 2000 agreed with the OCC's argument and blocked the municipal ATM-fee restrictions, prompting this month's hearing before a three-judge panel of the Ninth U.S. Circuit Court of Appeals. Opposing the OCC in that case, officials from California, New York and seven other states filed papers siding with the cities.

The OCC came to the defense of the same pair of big banks, among others, last year in Texas. The legislature there had recently passed a law that effectively prevented a bank from charging noncustomers a fee for cashing certain kinds of checks. Four big banks that operate in the state, including Wells Fargo, levy the fees, which typically range from $3 to $5 per check. Bank of America is planning to do the same. The four that currently charge the fees account for 40% of bank deposits in the state and generate a total of $5.2 million a year from the fees, according to court papers.

Before the new law was scheduled to take effect Sept. 1, Wells Fargo, Bank of America and Bank One Corp. of Chicago, which also holds a federal charter, asked the OCC if they had to obey the law. The OCC said they didn't. The agency weighed in with a "friend of the court" brief in U.S. district court in Austin, arguing that the National Bank Act permits national banks to charge whatever fees they deem appropriate for their services. In December, Judge James R. Nowlin agreed.

The Texas Banking Department is appealing the decision. "Texas passed a consumer-protection law that was duly enacted and should apply," says state Banking Commissioner Randall James.

The OCC even has backed its banks trying to knock down regulations that cover other companies they do business with outside of the banking industry.

In Michigan, the state Motor Vehicle Sales Finance Act, passed in 1950, requires that auto dealers fully disclose installment-payment terms. It also limits document-preparation fees to $40 and restricts the conditions under which

a car can be repossessed. The statute applies only to dealers who sell cars through installment plans. It doesn't apply to banks.

But National City Bank, a unit of Cleveland's National City Corp., and Huntington National Bank, owned by Huntington Bancshares Inc. of Columbus, Ohio, sought in administrative proceedings to make the dealers who market their car loans exempt from the law. Michigan's commissioner of financial and insurance services, Frank Fitzgerald, ruled in January 2000 that car dealers who teamed with national banks were still covered.

"We had to do something to get by that," says Daniel W. Morton, Huntington National's vice president and senior counsel. So the two banks asked the OCC for an opinion saying the state law was trumped by the National Bank Act. Commissioner Fitzgerald filed an objection, arguing that it would be "absurd" if the OCC could kill a state law aimed at nonbanking businesses.

In May, the OCC found otherwise, concluding that Michigan's law "frustrates the [banks'] ability to exercise their lending authority" and therefore shouldn't be enforced against car dealers marketing loans made by OCC-chartered banks. Michigan isn't contesting the ruling. The state doesn't think it can beat the OCC in federal court, says Mr. Fitzgerald.

Mr. Garsson, the OCC spokesman, says that consumers obtaining car loans funded by national banks -- such as those in the Michigan case -- would be covered by federal consumer protections that the OCC enforces.

In the FleetBoston case, the OCC received hundreds of letters from customers in 2000, complaining that the federally chartered bank had increased interest rates on its credit cards after allegedly promising a "fixed" rate. In response, the OCC sent customers letters saying it couldn't help. Federal law "recognizes banks' ability to change the terms of credit card account agreements," as long as the change is disclosed, the OCC said in a typical letter sent to a complaining customer on March 23, 2000. "If you wish to pursue further remedy to your complaint, we can only suggest that you contact private legal counsel regarding any additional remedies," the OCC added.

In October 2000, several customers filed suit, seeking class-action status and accusing FleetBoston of deceptive practices under Rhode Island state law. A Rhode Island state judge in Providence ruled in April that the case could proceed. But the OCC stepped in to help FleetBoston. The OCC argued in a friend-of-the-court brief that the state law on which the suit was based doesn't apply to FleetBoston because the OCC can take action against unfair and deceptive practices, as it did in the Providian case -- although the agency hadn't done so regarding FleetBoston.

Justice Judith Colenback Savage of Rhode Island Superior Court rejected the OCC's argument last April, a decision the state's Supreme Court declined to review. The case was then consolidated with a similar suit filed by a separate group of disgruntled FleetBoston customers before another Rhode Island judge.

In December, the new judge, Michael Silverstein, handed the OCC a victory. He ruled that FleetBoston couldn't be sued under the state's deceptive-practices law. Such a suit would call into question the OCC's "very foundational authority to regulate national banks," the judge ruled. At a hearing last week, FleetBoston sought to have the suit dismissed on those grounds. A decision is expected by the end of March.

(See related letter: "Letters to the Editor: Federal Regulatory Lapdogs" -- WSJ Feb. 8, 2002)

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Department of Banking and Finance
2990 Brandywine Road, Suite 200
Atlanta, Georgia 30341-5565
770-986-1633
www.gadbf.org

Sonny Perdue
Governor

David G. Sorrell
Commissioner

August 21, 2003

John D. Hawke, Jr.
Comptroller of the Currency
Independence Square
250 E. Street, SW
Washington, DC 20219-0001

RE: Recent Comptroller Preemption Determination of the Georgia Fair Lending Act (GAFLA)

Dear Mr. Hawke:

The Department has three follow-up issues regarding your July 30, 2003 preemption determination of the GAFLA. Leslie Bechtel, my Deputy Commissioner for Legal and Consumer Affairs, phoned Karen Solomon of your Washington office asking for Karen's return response to our questions on two issues of the preemption. Leslie had previously spoken to Mr. Mark Tenhunfeld of your Washington office, and Brenda Curry of your Southeast Regional Office regarding these issues. We request the OCC clarify the following issues in writing:

1. We have received conflicting information from various sources including your staff on what statutory provisions of GAFLA the OCC preempted. Please send us the Official Code of Georgia section citations that your July 30, 2003 Preemption Determination concludes are preempted. If it would be easier for you to provide the OCGA section citations that were not preempted, that listing would also be acceptable to answer this issue.
2. Because of the OCC's reference in the preemption determination to Gramm Leach Bliley Act and the insurance provisions under that federal act and because GAFLA's reference to the Georgia Department of Insurance as the enforcement authority over credit insurance products, we question whether credit life insurance falls under Gramm Leach Bliley Act and is therefore controlled under state law per Gramm Leach Bliley Act. Your answer to this query is requested.
3. Would mortgage loans originated by an external broker and subsequently funded by a national bank or national bank subsidiary be preempted by your July 30 preemption determination of GAFLA or would preemption only apply to mortgage loans originated by the national bank or national bank subsidiary? Your answer is requested.

John D. Hawke
Comptroller of the Currency
August 21, 2003
Page 2

Thank you in advance for your prompt response to this inquiry. If your staff has follow-up questions, please call Leslie Bechtel at 770-986-1650.

Sincerely,

David G. Sorrell

David G. Sorrell
Commissioner

DGS:sh

bcc: OCC Preemption File
David Sorrell
Leslie Bechtel
Susan Brown

Department of Banking and Finance

2990 Brandywine Road, Suite 200
Atlanta, Georgia 30341-5565
770-986-1633
www.gadbf.org

Sonny Perdue
Governor

David G. Sorrell
Commissioner

March 9, 2004

The Honorable John D. Hawke, Jr.
Office of the Comptroller of the Currency
250 E Street, SW
Public Information Room, Mailstop 1-5
Washington, D.C. 20219

Re: Response to Inquiry Regarding Preemption of Georgia Fair Lending Act

Dear Comptroller Hawke:

Since August 4, 2003, when we telephoned your offices, we have written, called, and reminded your office about questions we have on the sweeping preemption of Georgia law the OCC made on August 5, 2003 in the Federal Register. We have received replies that say nothing but that you needed to issue your subsequent preemption of all states' laws in January 2004 before you could answer Georgia questions.

That was done some time ago, and yet Georgia has never received one substantive answer to the three questions we asked. Ms. Williams indicated on January 8, 2004, that she would review our questions and respond "promptly". We have received nothing. Included for your information is a brief chronology of events.

I intend to pursue this lack of cooperation and response, but I wanted to give you the opportunity, again, to provide us with substantive answers to our questions. The questions about credit life insurance and liability of brokers are particularly pressing and timely.

Sincerely,

David G. Sorrell

David G. Sorrell
Commissioner

DGS:sh

cc: Julie Williams
Senator Saxby Chambliss
Senator Zell Miller
Representative Jack Kingston
Representative Stanford D. Bishop, Jr.
Representative Jim Marshall
Representative Denise Majette
Representative John Lewis
Representative John (Johnny) Isakson
Representative John Linder
Representative Michael Allen (Mac) Collins
Representative Charlie Norwood
Representative Nathan Deal
Representative Phil Gingrey
Representative Max Burns
Representative David Scott

Attachments (2)

July 30, 2003	OCC preemption of Georgia law
August 4, 2003	Telephone to Eric Thompson, referred to him by Mark Tenhunfeld, who did not answer our 3 questions. Thompson discusses, but requests further consultation with his fellow attorneys.
August 6, 2003	Karen Solomon calls - leaves message - Department Banking attorney returns call, leaves message.
August 21, 2003	Commissioner writes letter asking 3 questions (copy attached).
August 27, 2003	Department Banking attorney talks to Solomon - some disagreements between first discussion with Thompson and her response.
August 27, 2003 or shortly thereafter	Department attorney asks Solomon for written response.
September 9, 2003	Letter to Commissioner from Solomon, saying she is responsible for the response.
October 3, 2003	Georgia submits comments to large scale preemption.
October 4, 2003	No response received - letter sent asking when we can expect a response.
January 8, 2004	Letter from J. Williams - says final preemption could "supercede" our questions, therefore did rule making first. She will review questions and respond promptly.
February 2, 2004	No response.
March 8, 2004	No response.
March 9, 2004	Letter sent to Hawke, with copy to Julie Williams.

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

May 27, 2004

The Honorable Spencer Bachus
U.S. House of Representatives
Washington, DC 20515

Dear Congressman Bachus:

This letter is in response to a number of questions you raised about the New Basel Capital Accord (Basel II) following the April 1 oversight hearings before the House Committee on Financial Services. I welcome the opportunity to respond to your questions.

The specific questions your staff forwarded after the April 1 hearing fall into three broad categories – complexity and status of Basel Committee negotiations, potential competitive implications, and the extent to which the development of Basel II is being driven by the need to improve supervision in foreign jurisdictions. Each question is reproduced below in italics, followed by my response.

- *[Y]ou have stated . . . that you are very concerned over the state of the Basel II negotiations and the complexity of the proposed accord. Have there been any improvements to Basel II over the past several months that have changed your mind on this issue? Are you still concerned that OCC and other bank examiners may not be able to implement this complex framework? If so, what is the solution? Is it better to walk away and not update the existing regulatory capital framework for banks than to try to implement the Basel proposal?*

Largely at the initiative of the U.S. agencies, there have been numerous significant improvements in the Basel II proposals over the past several months. These improvements reflect a thorough and rigorous deliberative process that includes ongoing consideration of public comments on the earlier Basel proposals and on the Advanced Notice of Proposed Rulemaking (ANPR) that we issued in the U.S. last summer. As I indicated in my April testimony, one of the most significant of these issues – and one that U.S. banks were virtually unanimous in criticizing in response to the Basel Committee's third consultative paper (CP-3) – involved the fundamental question of what losses capital requirements should be designed to cover. CP-3 would have calibrated capital to ensure coverage of both expected losses (EL) plus unexpected losses (UL). However, banks in the U.S. today generally measure and manage their internal economic capital allocations by reference to UL only, and most banks rely on a combination of reserves and credit pricing to cover EL. As we examined this issue, we became convinced not

only that the banks were conceptually correct in their arguments, but that retaining the EL plus UL calibration would have severe ramifications – not the least of which might be to seriously jeopardize the industry's acceptance of Basel II framework as being a conceptually sound framework. While many on the Basel Committee resisted this initially, the Committee ultimately put forth a new proposal in October to modify the calibration of Basel II to UL only. This modification was strongly endorsed by industry participants and has now been adopted by the Committee.

The Committee announced several other important modifications to CP-3 in January that are responsive to numerous comments we received on CP-3 and the U.S. agencies' ANPR. These modifications include simplifying the proposed treatment for securitizations and aligning it more closely to industry practice and an agreement to find a prudentially sound solution that better recognizes credit mitigation techniques used by the industry.

At its most recent meeting this month, the Committee resolved one of its most difficult remaining policy issues, relating to the appropriate risk-based capital treatment of certain retail credit products – unused credit card lines in particular. This issue is critically important for national banks and for the cost and availability of consumer credit. It is also an area in which consensus was not easy to achieve. However, given the prominence of this issue for U.S. banks, and for national banks in particular, there was little room for substantive compromise. The OCC is pleased that the agreed-upon solution is one that does not appear likely to unduly disrupt or disadvantage established, well-functioning business practices.

Of course, each of these issues, as well as other provisions of the Basel II package, will be again subject to full notice and comment in the U.S. before they take effect as a final rule. When the Basel II agreement is finalized, we will launch our more in-depth domestic deliberative process. This process will include a fourth quantitative impact study (QIS4) and a joint notice of proposed rulemaking (NPR). A more detailed discussion of our deliberative process is provided in the response to the next question.

Another significant development at the Basel Committee's May meeting is a decision to defer for one year the implementation of Basel II "advanced approaches," which are the approaches we plan to use in the U.S. This additional time will help banks and supervisors make adequate preparations to implement and oversee the new capital framework. Within the U.S., these preparations will include additional examiner training, supervisory guidance and examination procedures on Basel II. The guidelines and procedures will provide more explicit and detailed "roadmaps" for the industry and examiners for implementing and evaluating the various risk management and measurement components that will be required under Basel II. With these additional tools, I am confident that our examiners will be able to oversee and evaluate banks' implementation of Basel II.

In my view, the improvements we have seen to date, coupled with a process that will allow continued responsiveness to industry concerns, make it unnecessary to consider whether to simply "walk away" at this point. I have always maintained that if we find additional changes are needed, we will insist on those changes being made. Recent events have shown that our

domestic consultation process works, and I have every confidence it will continue to be productive.

- *One of the things that concerns me the most about the Basel II proposal is the potential impact that it could have on competition in the U.S. banking market. Might medium sized financial institutions be negatively affected if they do not become Basel II-compliant? Do you believe this proposal would widen the gap between large and medium institutions, forcing consolidations and setting up some banks as acquisition targets? Would such consolidation occur even without changes in the regulatory capital framework?*

One of the major outstanding issues the Basel Committee still must tackle is the final calibration of the resulting regulatory capital charges, and this issue will clearly have a bearing on the competitive impact of Basel II.

Closely related to the calibration issue, the U.S. agencies will conduct a fourth quantitative impact study (QIS 4) before issuing a Notice of Proposed Rulemaking (NPR), which will once again seek public comment on U.S. implementation of Basel II. We intend QIS 4 to be significantly more reliable than the Basel Committee's earlier quantitative impact studies, and the results should be far more useful than any data we currently have in determining the magnitude of the impact of Basel II on bank capital and potential competitive inequities, as well as determining ultimately what to do about them.

Moreover, OCC staff have made a preliminary determination that the implementation of Basel II for national banks will be a "significant regulatory action" for purposes of Executive Order 12866. Consequently, we will prepare and submit an economic analysis to the Office of Management and Budget's Office of Information and Regulatory Affairs (OIRA). That analysis will include:

- a description of the need for the rules and an explanation of how they will meet the need;
- an assessment of the benefits anticipated from the rules together with, to the extent feasible, a quantification of those benefits;
- an assessment of the costs anticipated from the rules together with, to the extent feasible, a quantification of those costs; and
- an assessment of potentially effective and reasonably feasible alternatives to the planned regulation, and why the planned regulatory action is preferable to the identified potential alternatives.

We have begun discussions with OIRA regarding the how these analyses will be designed and conducted.

With regard to the consolidation that we are seeing within the banking industry, I would note that there are a myriad of factors that play into a bank's decision about possible mergers or acquisitions. These include general operating efficiencies, economies of scale and synergies that may be gained from leveraging delivery, back office and risk management technologies, irrespective of regulatory capital requirements.

- *Some have argued that U.S. regulators are using the Basel II requirements as an indirect method for improving banking regulation and oversight in foreign countries. The idea, we understand, is that specific quantitative regulatory requirements would require foreign regulators to improve substantially the quality of their supervisory processes. This is particularly problematic if the final global standard would have a detrimental impact on U.S. banks. Can you comment on this assertion? Is it true that a main motivation for negotiating the new capital framework was to increase regulatory standards and capacity outside the United States? Might other means, such as dialogue, be more effective in achieving this goal with less impact on the entire U.S. banking system?*

My concern, and that of the OCC, has always been first and foremost to improve risk management practices and supervisory processes for national banks in the U.S. A crucial priority in our approach to Basel II has been to first do no harm. While there will always be an element of give and take in any kind of extensive international deliberations, I believe the current Basel II proposals are fully consistent with those priorities. I have been vocal at times about the gap in supervision that exists between the U.S. and many other countries, including some Basel Committee members. I have made that point repeatedly in explaining why we might reject certain provisions that do not meet our "do not harm" standard and which we deem unnecessary because of the unique nature of supervision in the U.S. I have not felt it appropriate, however, to use Basel II as a lever to force changes on other jurisdictions. While I believe the U.S. is a clear leader by example in this area, I also believe that effective supervision requires a commitment that goes far beyond rigid compliance with a set of specified rules. More generally, I believe that efforts that lead to improved risk management practices among global financial institutions benefits the U.S. financial sector by providing a more stable and sound global banking system.

*   *   *

In closing, I would like to assure you that the OCC and the other U.S. agencies remain mindful of the issues and concerns you and other members of Congress have raised previously with Basel II. In particular, we continue to seriously consider the issues raised in a November 3, 2003 letter signed by you and ten other members of the Committee on Financial Services. I believe that to the extent those concerns can be practicably addressed within the Basel Committee itself, we have made significant progress. However, as you recently noted following the consensus announced by the Basel Committee on May 11, "the committee's final list of outstanding issues is incomplete compared to the actual concerns that face the American banking industry." I believe there are a number of issues for which the Basel Committee is not the ideal forum to reach definitive closure and that the remaining issues that have not been taken up by the Basel Committee can be more satisfactorily addressed through our domestic rulemaking and implementation processes.

You also recently reiterated your concerns about capital charges for operational risk. As the Basel II proposals have evolved, the OCC has consistently voiced concern about the treatment of operational risk. We believe, however, that the most current iteration of the operational risk proposal, the Advanced Measurement Approaches (AMA), is a significant improvement over

earlier proposals. Institutions using the AMA will have considerable flexibility to develop operational risk management and measurement systems appropriate to the nature of their activities, business environment, product mix, and internal control structure. Based on these and other improvements, I am persuaded that operational risk should be addressed in Basel II. With that said, however, we continue to work with the industry and other interested persons to address remaining concerns with the AMA, and to further clarify certain aspects of U.S. implementation to alleviate those concerns.

As indicated above, a large amount of substantive process lies ahead of us in the U.S. The results of our QIS-4 exercise, the Executive Order 12866 analyses, and future notice and comment procedures will tell us much about the balance of costs and complexity, the currently unknown competitive implications, and the extent to which we have achieved our objective of greater risk sensitivity in the capital regime without causing undue or unwarranted disruptions in well-established and well-functioning markets. We are committed to being satisfied on those fronts before final implementation of Basel II can occur in the U.S.

I trust this is responsive to your inquiry. Each of the U.S. agencies remains mindful of Congressional interest in this deliberative process, and we plan to continue to engage in frequent communication between our staffs and the staff of the Committee on Financial Services on these matters. Continuing this dialogue will facilitate addressing serious policy issues substantively and in a manner consistent with our respective responsibilities.

Sincerely,

John D. Hawke, Jr.

John D. Hawke, Jr.
Comptroller of the Currency

SUPPLEMENTAL RESPONSES BY THE OCC TO COMMITTEE MEMBERS' QUESTIONS AT THE APRIL 1, 2004 HEARING ON OCC OVERSIGHT

1. **In response to a question from Rep. Garrett regarding the supervision of foreign-based service providers:**

The OCC has the authority to examine and supervise the services performed for a national bank by a foreign-based service provider to the same extent as if such services were being performed by the bank itself. Our principal supervisory strategy in this area is to focus on the ability and obligation of the serviced national bank to develop and implement a comprehensive risk management process to oversee its foreign-based service providers. Our supervisory approach emphasizes the responsibility of the serviced financial institution to conduct adequate due diligence before entering into a contract, manage risks appropriately, comply with applicable laws, and ensure access to critical information with respect to the services being provided, whether by a foreign-based or domestic entity.

Therefore, our review of foreign-based service provider arrangements to date has been focused on interviewing institution staffs and reviewing documentation (security policies, third-party security audits, financial statements, contracts, business resumption and disaster recovery plans, etc.), which must be maintained in English at a domestic office of the institution. We maintain relationships with foreign bank supervisors and may seek information on foreign-regulated service providers through the appropriate supervisory agency in the servicer's home country. If circumstances warrant, we can and will exercise our authority to examine services performed by foreign-based service providers.

2. **In response to a question from Rep. Bachus regarding grace periods for credit card payments:**

The issue is governed by the Truth in Lending Act (15 U.S.C. § 1601 et seq.) and Regulation Z of the Board of Governors of the Federal Reserve System (12 C.F.R. Part 226). The Truth in Lending Act provides that, *if* a credit card agreement provides for a grace period, the credit card bill must be mailed to the consumer at least 14 days prior to the expiration of the grace period. Because the grace period is an item required to be disclosed in the credit card issuer's initial disclosure statement, any change in the grace period would require a 15-day advance written notice to the consumer.

3. **In response to a question from Rep. Kelly regarding the caseload of compliance examiners:**

The OCC currently has 107 compliance specialist examiners, many of whom are assigned to banks in our Large Bank and Mid-Size Bank programs. For our largest banks, compliance specialists are assigned exclusively to that bank. There are 25 Large Banks where that is the case, involving the exclusive assignment of 54 compliance specialists. In other situations, a compliance specialist will have responsibilities for more than one bank, with the number varying depending on the size and complexity of the banks involved. Because bank examinations are

conducted by business line rather than by corporate structure, OCC examiners assigned to a given bank are also responsible for compliance by that bank's operating subsidiary.

4. **In response to a request by Rep. Waters for the number of enforcement actions against national banks and their operating subsidiaries related to abusive real estate lending practices:**

Evidence of abusive real estate lending practices by national banks is scant, but in those instances where abusive practices are identified, our record shows that we act forcefully to protect consumers, and we do so using traditional as well as innovative approaches designed to prevent national banks from engaging in abusive lending practices and to remedy such practices if they have occurred.

The OCC was the first federal banking agency to take enforcement action against an institution it supervises for violations of section 5 of the Federal Trade Commission Act (FTC Act), which prohibits unfair and deceptive practices. In a precedent setting enforcement action against Providian National Bank in 2000, the OCC cited violations of section 5 of the FTC Act *and* the California state unfair trade practices law as the basis for obtaining affirmative remedies from the bank, including consumer restitution and a cease and desist order. Notably, the OCC ordered the bank to pay affected consumers *nationwide* more than $300 million in restitution.

Since our cease and desist agreement with Providian, the OCC has brought other actions based on violations of section 5 of the FTC Act to address not only deceptive practices with respect to consumer credit, but also *unfair* practices. These enforcement actions have resulted in millions of dollars in restitution for consumers. No other federal banking agency has employed section 5 of the FTC Act to obtain monetary and other relief for consumers harmed by practices that are not otherwise specifically prohibited by federal law.

In addition, we moved aggressively against national banks for engaging in payday lending programs that involved consumer abuses and unsafe and unsound practices. We took enforcement action against the four national banks that had entered into contracts with payday lending concerns and ordered the banks to cease offering payday loans by terminating the relationship with the third party lender. As a result of our actions, no national bank is engaging in any such payday lending relationships in any community in the United States.

The OCC conducts in-depth examinations of national banks and national bank operating subsidiaries for compliance with a host of laws that protect consumers from abusive practices in connection with real estate (and other) loan transactions. These examinations review for compliance with the Home Ownership and Equity Protection Act (HOEPA), Truth in Lending Act (TILA), Equal Credit Opportunity Act (ECOA), Fair Housing Act, Real Estate Settlement Procedures Act (RESPA), and Flood Disaster Protection Act, among other laws, and for compliance with OCC regulations. These federal laws contain not only highly technical compliance requirements, but also substantive provisions that are essential to protecting consumers against abusive or misleading credit practices in their consumer and home loan transactions. Through our compliance examinations, we have detected and addressed several

hundreds of violations of various provisions of these laws, including in connection with mortgage loans.

Our consumer protection supervision does not stop at the conclusion of the compliance examination. The OCC also acts to ensure that national banks and their operating subsidiaries *correct* any violations that have been cited in a report of examination. Depending upon the nature of the violation and the extent of noncompliance, appropriate corrective action can range from ensuring that bank policies and procedures are changed, taking informal enforcement actions, and directing the bank to pay restitution for consumers, to initiation of formal enforcement actions such as imposing civil money penalties and cease and desist orders.

One formal enforcement action we took recently with respect to real estate loans was to charge Clear Lake National Bank with violating HOEPA, TILA, RESPA, and the FTC Act for unfair practices involving mortgage loans used to pay off tax liens on borrowers' homes. This is the only instance in which a federal banking agency has charged a bank (or savings association) with *unfair* practices in connection with mortgage lending in violation of the FTC Act. A formal enforcement action was necessary in this matter to address the serious deficiencies we found in our compliance examination, and to obtain appropriate and comprehensive relief for consumers who were the victims of predatory lending practices by the bank. As a result of our enforcement action, the bank was required to make a full refund of all fees *and interest* paid by each consumer who was harmed by the unfair and abusive lending practices. It is important to note that the OCC is committed to using all of the enforcement tools at its disposal, including the FTC Act and state unfair and deceptive practices laws, to address any future instances of unfair and abusive lending practices that we may find.

We have prepared a chart that describes nineteen formal enforcement actions by the OCC in the past five years to address consumer protection concerns. However, the number of enforcement actions is not, by itself, the sole measurement of the breadth and scope of the OCC's consumer protection activities. When the OCC identifies weaknesses in a national bank's compliance practices, a range of actions can be taken to address the deficiencies and to obtain relief for consumers. While formal enforcement actions clearly are an important aspect of our supervisory process, they are not required in every circumstance, and where violations of a more technical nature are cited, the bank may be required to take corrective and remedial action through more informal processes. Nevertheless, as the chart clearly demonstrates, the OCC will use its formal enforcement authority wherever it is necessary to obtain appropriate corrective action by the bank and to obtain customer redress.

OFFICE OF THE COMPTROLLER OF THE CURRENCY
RECENT CONSUMER PROTECTION ENFORCEMENT ACTIONS

Bank or Company Name	Action/Date	Affirmative Actions Required	Monetary Relief Obtained for Consumers
First USA Bank, N.A. Wilmington, Delaware	Safety and Soundness Notice of Deficiency 12/16/99	Change policies, procedures, systems and controls, and make restitution to affected consumers.	Approximately $10 million in restitution paid to approximately 1.28 million consumers.
Providian National Bank, Tilton, New Hampshire	Cease and Desist Order 6/28/00	Change marketing practices, policies and procedures, and make restitution to affected consumers.	Approximately $304 million in restitution paid to approximately 5.4 million consumers.
United Credit National Bank, Sioux Falls, South Dakota	Cease and Desist Orders 2/25/00 & 6/29/00	Closed credit card program and required Bank to liquidate at no loss or cost to the FDIC.	Satisfied all consumers' claims (number and amount unknown).
UICI (controlling shareholder of United Credit National Bank)	Cease and Desist Order 6/29/00	Provide funds to pay for consumers' claims, pay off deposits, and liquidate United Credit National Bank at no loss or cost to the FDIC.	Provided funds to United Credit National Bank to pay for consumers' claims (number and amount unknown) and pay off deposits.
United CreditServ, Inc. (controlling shareholder of United Credit National Bank)	Cease and Desist Order 6/29/00	Provide funds to pay for consumers' claims, pay off deposits, and liquidate United Credit National Bank at no loss or cost to the FDIC.	Provided funds to United Credit National Bank to pay for consumers' claims (number and amount unknown) and pay off deposits.
net 1st National Bank, Boca Raton, Florida	Cease and Desist Order 9/25/00	Change marketing practices related to its "Pay as You Go" credit card program.	No restitution required.
Direct Merchants Credit Card Bank, N.A. Scottsdale, Arizona	Cease and Desist Order 5/3/01	Change marketing practices and make restitution to affected consumers.	Approximately $3.2 million in restitution paid to approximately. 62,000 consumers.
First National Bank of Marin, Las Vegas, Nevada	Cease and Desist Order 12/3/01	Change marketing practices and make restitution to affected consumers.	Approximately $3.9 million in restitution paid to approximately 61,000 consumers.
Eagle National Bank, Upper Darby, Pennsylvania	Cease and Desist Order 12/18/01	Cease making payday loans.	No restitution required.
First National Bank, Ft. Pierre, South Dakota	Formal Agreement 7/18/02	Change marketing practices.	No restitution required.

OFFICE OF THE COMPTROLLER OF THE CURRENCY
RECENT CONSUMER PROTECTION ENFORCEMENT ACTIONS
(Continued)

Bank or Company Name	Action/Date	Affirmative Actions Required	Monetary Relief Obtained for Consumers
Goleta National Bank, Goleta, California	Cease and Desist Order 10/28/02 Civil Money Penalty Order 10/28/02	Cease making payday loans, notify consumers of missing loan files, and assessed civil money penalty in the amount $75,000.	No restitution required.
ACE Cash Express, Inc. (Contacted by AGs in Colorado and North Carolina)	Cease and Desist Order 10/25/02 Civil Money Penalty Order 10/25/02	Cease payday lending through national banks, and assessed civil money penalty in the amount of $250,000.	No restitution required.
First National Bank in Brookings, Brookings, South Dakota	Cease and Desist Order 1/17/03	Cease making payday loans, change marketing practices regarding credit card solicitations, and make restitution to affected consumers.	Approximately $3.1 million in restitution paid to approximately 34,000 consumers.
Peoples National Bank, Paris, Texas	Cease and Desist Order 1/30/03 Civil Money Penalty Order 1/30/03	Cease making payday loans and assessed civil money penalty in the amount of $175,000.	No restitution required.
Advance America, Inc.	Cease and Desist Order 1/29/03	Cease payday lending through national banks.	No restitution required.
Household Bank (SB), National Association, Las Vegas, Nevada	Formal Agreement 3/25/03	Change marketing practices on financing sales of air conditioning units.	Approximately $5 million in restitution paid to approximately 1,230 consumers.
First Consumers National Bank, Beaverton, Oregon (Oregon AG made a referral for a portion of the problems)	Formal Agreement 7/31/03	Make restitution to affected consumers.	Approximately $1.7 million in restitution paid to approximately 39,000 consumers.

OFFICE OF THE COMPTROLLER OF THE CURRENCY
RECENT CONSUMER PROTECTION ENFORCEMENT ACTIONS
(Continued)

Bank or Company Name	**Action/Date**	**Affirmative Actions Required**	**Monetary Relief Obtained for Consumers**
Clear Lake National Bank, San Antonio, Texas	Cease and Desist Order 11/7/03	Change lending practices, and make restitution to affected consumers.	Paid approximately $288,000 in restitution to 60 consumers.
First National Bank of Marin, Las Vegas, Nevada	Cease and Desist Order 5/24/04	Change marketing practices, cease providing certain types of credit cards, and make restitution to affected consumers.	Bank is in progress of repaying customers - estimated to be in excess of $1 million in restitution to 130,000 consumers.

5. **In response to a request from Rep. Miller of North Carolina for the number of OCC enforcement actions in 2003, and studies examining effects of the North Carolina anti-predatory lending law:**

OCC Formal Enforcement Actions
For 2003

	Bank Name	Bank City	State	Charter Number	First Name	Last Name	Type	Amount	Completion Document	Issues
1	Advance America, Cash Advance Center, Inc.	Spartanburg	SC				C&D		2003-3	Books, Consumer Laws
2	AMCORE Bank, N.A.	Rockford	IL	13652			BCMP	5,000	2003-111	Flood
3	American Investment Bank, National Association	Salt Lake City	UT	18174			FA		2003-22	Capital, Management, IT, Planning
4	Americana National Bank	Albert Lea	MN	10903			C&D		2003-58	Affiliate/Insider Transactions, Audit, BSA, Books, Conflicts, Compensation, Loan, IRR
5	Bank of America, N.A.	Charlotte	NC	13044	Kristen	Anderson	REM		2003-128	Embezzlement
6	Bank of America, N.A.	Charlotte	NC	13044	Connie	Jones-Kennedy	REM		2003-36	Loan
7	Bank of America, N.A.	Charlotte	NC	13044	William F.	Lackner	REM		2003-55	Embezzlement
8	Bank of America, N.A.	Charlotte	NC	13044	Paul	Zolezzi	REM		2003-147	Embezzlement
9	Bank of America, National Association	Charlotte	NC	13044	Keisha	Davis	REM		2003-35	Forgery
10	Bank of China	Los Angeles	CA	80096			C&D		2003-125	BSA, Loan, IT, Books, Audit
11	Bank of China	New York	NY	80028			C&D		2003-125	BSA, Loan, IT, Books, Audit
12	Bank of China	New York	NY	80091			C&D		2003-125	BSA, Loan, IT, Books, Audit
13	Bank of Communications	New York	NY	80107			FA		2003-11	BSA, Loan, Management, IT, Planning
14	Bank of Communications	New York	NY	80107	Stephen	Lee	PC&D		2003-145	BSA
15	Bank One, N.A.	Chicago	IL	8	Wendy A.	Webb	REM		2003-34	Identity Theft
16	Bank One, NA	Columbus	OH	7621	Bianca C.	Hall	REM		2003-158	Embezzlement
17	Bridgeview Bank, N.A.	Oklahoma City	OK	17076	Sidney R.	Carey	REM		2003-106	Loan Fraud
18	Broadway National Bank	New York	NY	20622	Daniel	Cardone	CMP	35,000	2003-113	BSA
19	Broadway National Bank	New York	NY	20622	Sam	Chung	CMP	35,000	2003-112	BSA
20	Capital Management Investors Holdings, Inc.	Chicago	IL				C&D		2003-137	Investments, Planning, Capital, Liquidity, Trust
21	Chase Bank of Texas, N.A.	Houston	TX	500373	Byron A.	Coston	PC&D		2003-57	Embezzlement
22	Chase Bank of Texas, N.A.	Houston	TX	500373	Byron A.	Coston	REM		2003-57	Embezzlement
23	Chase Bank of Texas, N.A.	Houston	TX	500373	Byron A.	Coston	REST	18,749.68	2003-57	Embezzlement
24	Chase Bank of Texas, NA	Houston	TX	500373	Damion D.	Robertson	PC&D		2003-61	Embezzlement
25	Citibank, N.A.	New York	NY	1461			FA		2003-77	Planning, Controls, Loan, Audit
26	Citibank, N.A.	Bayamon	PR	1461	Benedicta	Arocho-Burgos	REM		2003-93	Embezzlement
27	Citizens National Bank & Trust of Hazard	Hazard	KY	22988	L.D.	Gorman	CMP	69,000	2003-8	Conflicts
28	Citizens National Bank & Trust of Hazard	Hazard	KY	22988	Dewey	Gorman	CMP	46,000	2003-7	Conflicts
29	Citizens National Bank & Trust of Hazard	Hazard	KY	22988	Dewey	Gorman	REM		2003-7	Conflicts
30	Citizens National Bank & Trust of Hazard	Hazard	KY	22988	L.D.	Gorman	REM		2003-8	Conflicts
31	Citizens National Bank of Albion	Albion	IL	14435	Gregory J.	Hanneken	REST	20,947.52	2003-159	Loan
32	Clear Lake National Bank	San Antonio	TX	23711			C&D/REST	288,000	2003-135	Consumer Laws, UDAP, Bank Restitution
33	Clear Lake National Bank	San Antonio	TX		Nancy A.	Kinder	CMP	10,000	2003-153	Consumer Laws, UDAP
34	Clear Lake National Bank	San Antonio	TX		Nancy A.	Kinder	PC&D		2003-153	Consumer Laws, UDAP
35	CoreStates Financial	Philadelphia	PA		Marian L.	Butler	REM		2003-164	Embezzlement

	Bank Name	Bank City	State	Charter Number	First Name	Last Name	Type	Amount	Completion Document	Issues
36	Cumberland Valley National Bank & Trust Company	East Bernstadt	KY	10254			BCMP	14,000	2003-13	ALLL
37	Delta National Bank	Manteca	CA	16154	Toinette	Rossi	CMP	45,000	2003-59	Loan Fraud
38	Delta National Bank	Manteca	CA	16154	Andrew	Rossi	CMP	100,000	2003-80	Loan Fraud
39	Delta National Bank	Manteca	CA	16154	Toinette	Rossi	PC&D		2003-59	Loan Fraud
40	Delta National Bank	Manteca	CA	16154	Andrew	Rossi	REM		2003-80	Loan Fraud
41	Dillard National Bank	Gilbert	AZ	18777			FA		2003-161	Liquidity
42	Dillard National Bank	Gilbert	AZ	18777			FA		2003-142	Planning, Liquidity, Affiliate/Insider Transactions, Books, Audit, Info. Security, IT, Third Party Servicer
43	Farmers and Merchants National Bank of Nashville	Nashville	IL	8221			FA		2003-5	Planning, Loan, Management
44	Farmers National Bank	Walton	KY	22928			FA		2003-21	Planning, Management, Loan, Affiliate/Insider Transactions, Conflicts, Liquidity, Audit, Capital
45	First Central Bank McCook, National Association	McCook	NE	23734			FA		2003-144	Planning, Loan, ALLL, IRR
46	First Community Bank, N.A.	Olney	IL	22865	Wayne H.	Benson	CMP	8,000	2003-139	BSA
47	First Community Bank, N.A.	Olney	IL	22865	Wayne H.	Benson	PC&D		2003-139	BSA
48	First Community Bank, N.A.	Olney	IL	22865	Kevin Brent	Washburn	CMP	25,000	2003-151	Loan
49	First Community Bank, N.A.	Olney	IL	22865	Kevin Brent	Washburn	REM		2003-151	Loan
50	First Consumers National Bank	Beaverton	OR	21688			C&D		2003-39	Third Party Servicer
51	First Consumers National Bank	Beaverton	OR	21688			FA/REST	1,700,000	2003-100	UDAP, Bank Restitution, Third Party Servicer
52	First National Bank	Denver City	TX	17365	Teresa Scott	Moyers	REM		2003-94	Embezzlement
53	First National Bank	Denver City	TX	17365	Deborah Jean	Winfrey	REM		2003-95	Embezzlement
54	First National Bank - Colorado	Fowler	CO	7637			FA		2003-162	BSA, CC, Loan, Capital
55	First National Bank & Trust	Kokomo	IN	14519			BCMP	5,000	2003-103	Flood
56	First National Bank and Trust	Phillipsburg	KS	3601	Lloyd K.	Culbertson	CMP	3,000	2003-83	Loan, Compensation
57	First National Bank and Trust	Phillipsburg	KS	3601	Katherine	Culbertson	CMP	2,000	2003-82	Loan, Compensation
58	First National Bank and Trust	Phillipsburg	KS	3601	William W.	Kaumans	CMP	2,000	2003-84	Loan, Compensation
59	First National Bank and Trust	Phillipsburg	KS	3601	Jaret	Moyer	CMP	2,000	2003-86	Loan, Compensation
60	First National Bank and Trust	Phillipsburg	KS	3601	Charles I.	Moyer	CMP	2,000	2003-85	Loan, Compensation
61	First National Bank and Trust	Phillipsburg	KS	3601	Doyle D.	Rahjes	CMP	2,000	2003-87	Loan, Compensation
62	First National Bank and Trust	Phillipsburg	KS	3601	William H.	Smith	CMP	2,000	2003-88	Loan, Compensation
63	First National Bank in Brookings	Brookings	SD	12838			C&D/REST	3,100,000	2003-1	UDAP, Bank Restitution, Third Party Servicer, Management, Conflicts, Merchant Processing
64	First National Bank in Homer	Homer	IL	11882			FA		2003-156	Planning, Management, Conflicts, Loan
65	First National Bank of Coffee County	Douglas	GA	22327	Jeffery W.	Johnson	CMP	15,000	2003-62	Loan, Affiliate/Insider Transactions
66	First National Bank of Gaylord	Gaylord	MI	16477			FA		2003-90	Loan, Management, Audit, IT, Planning, Capital, A/L, IRR
67	First National Bank of Herminie	Hermitage	PA	24283	Nancy J.	Cross	REM		2003-56	Identity Theft
68	First National Bank of Keystone	Keystone	WV	10369		Kutak Rock LLP	FA		2003-45	Third Party Servicer

	Bank Name	Bank City	State	Charter Number	First Name	Last Name	Type	Amount	Completion Document	Issues
69	First National Bank of Keystone	Keystone	WV	10369	Michael T.	Lambert	FA		2003-46	Third Party Servicer
70	First National Bank of Littlefield	Littlefield	TX	12824			C&D		2003-15	Planning, Liquidity, Loan
71	First National Bank of Littlefield	Littlefield	TX	12824	James T.	Lee	PC&D		2003-15	Planning, Liquidity, Loan
72	First National Bank of Lubbock	Lubbock	TX	18479	Charles	Cleveland	CMP	2,000	2003-25	Loans, RM, Capital
73	First National Bank of Lubbock	Lubbock	TX	18479	Robert C.	Hobgood	CMP	2,000	2003-26	Loans, RM, Capital
74	First National Bank of Northern Kentucky	Fort Mitchell	KY	22439			C&D		2003-14	Capital, Planning, Management, Loan, ALLL, Audit, Liquidity, IRR, CC, BSA, IT, Third Party Servicer
75	First National Bank of Northern Kentucky	Fort Mitchell	KY	22439	Richard M.	Thomas	CMP	10,000	2003-140	Loan Fraud
76	First National Bank of Northern Kentucky	Fort Mitchell	KY	22439	Richard M.	Thomas	REM		2003-140	Loan Fraud
77	First National Bank of Northern Kentucky	Fort Mitchell	KY	22439	Richard M.	Thomas	REST	50,000	2003-140	Loan Fraud
78	First National Bank of O'Donnell	O'Donnell	TX				C&D		2003-70	Planning, Affiliate/Insider Transactions, Capital, Books
79	First National Bank of O'Donnell	O'Donnell	TX		Nelson D.	Hogg	REM		2003-72	Embezzlement
80	First National Bank of Osceola County	Kissimmee	FL	21730			FA		2003-4	BSA
81	First National Bank of Osceola County	Kissimmee	FL	21730	Jackie	Davidson	PC&D		2003-10	BSA
82	First National Bank of Paonia	Paonia	CA	6671			FA		2003-155	ALLL, Capital, Loan, Merchant Processing, Participations Purchased
83	First National Bank of Wiggins	Wiggins	MS	16204			C&D		2003-78	Planning, Capital, Management, ALLL, IT, BSA, CC, Audit, Loan, Liquidity, A/L, Loan
84	Fleet National Bank	Providence	RI	500327	Timothy	Benson	REM		2003-119	Embezzlement
85	Fleet National Bank	Providence	RI	500327	Timothy	Benson	REST	910	2003-119	Embezzlement
86	Forrest City Bank, N.A.	Forrest City	AR	23195			FA		2003-102	Capital, Planning, Management, Loan, ALLL, CC
87	Fremont National Bank & Trust	Fremont	NE	2848			BCMP	5,000	2003-166	Flood
88	Gateway National Bank	St. Louis	MO	15521			FA		2003-104	Management, Controls, Audit, Loan, CC
89	Grand Valley National Bank	Grand Junction	CO	18058	Vicki L.	Boutilier	CMP	10,000	2003-19	Identity Theft
90	Grand Valley National Bank	Grand Junction	CO	18058	Vicki L.	Boutilier	PC&D		2003-19	Identity Theft
91	Grand Valley National Bank	Grand Junction	CO	18058	Vicki L.	Boutilier	REM		2003-19	Identity Theft
92	Grand Valley National Bank	Grand Junction	CO	18058	James Earl	Smith	CMP	20,000	2003-20	Identity Theft
93	Grand Valley National Bank	Grand Junction	CO	18058	James Earl	Smith	PC&D		2003-20	Identity Theft
94	Grand Valley National Bank	Grand Junction	CO	18058	James Earl	Smith	REM		2003-20	Identity Theft

	Bank Name	Bank City	State	Charter Number	First Name	Last Name	Type	Amount	Completion Document	Issues
95	Guaranty National Bank of Tallahassee	Tallahassee	FL	21162			C&D		2003-37	Consumer Laws, Planning, Capital Management, Loan, ALLL, Audit, CC, Third Party Servicer
96	Guaranty National Bank of Tallahassee	Tallahassee	FL	21162			BCMP	25,000	2003-81	
97	Hamilton Bank, N.A.	Miami	FL	17675	Antonio	Arbulu	CMP	10,000	2003-60	Loan, Examination Obstruction
98	Hamilton Bank, N.A.	Miami	FL	17675	Antonio	Arbulu	PC&D		2003-60	Loan, Examination Obstruction
99	Hamilton Bank, N.A.	Miami	FL	17675	Carlos	Bernace	CMP	40,000	2003-122	Loan, Affiliate/Insider Transactions, Conflicts, Books, Examination Obstruction
100	Hamilton Bank, N.A.	Miami	FL	17675	Carlos	Bernace	REM		2003-122	Loan, Affiliate/Insider Transactions, Conflicts, Books, Examination Obstruction
101	Hamilton Bank, N.A.	Miami	FL	17675	Carlos	Bernace	REST	210,000	2003-122	Loan, Affiliate/Insider Transactions, Conflicts, Books, Examination Obstruction
102	Hamilton Bank, N.A.	Miami	FL	17675	Alina	Cannon	PC&D		2003-41	Loan Fraud
103	Hamilton Bank, N.A.	Miami	FL	17675	Ronald	Lacayo	CMP	40,000	2003-52	Loan
104	Hamilton Bank, N.A.	Miami	FL	17675	Ronald	Lacayo	REM		2003-52	Loan
105	Hamilton Bank, N.A.	Miami	FL	17675	Eduardo	Masferrer	CMP	40,000	2003-150	Loan, Affiliate/Insider Transactions, Conflicts, Books, Examination Obstruction
106	Hamilton Bank, N.A.	Miami	FL	17675	Eduardo	Masferrer	REM		2003-150	Loan, Affiliate/Insider Transactions, Conflicts, Books, Examination Obstruction
107	Hamilton Bank, N.A.	Miami	FL	17675	Eduardo	Masferrer	REST	960,000	2003-150	Loan, Affiliate/Insider Transactions, Conflicts, Books, Examination Obstruction
108	Household Bank (SB), National Association	Las Vegas	NV	22675			FA/REST	5,000,000	2003-17	UDAP, Bank Restitution, Third Party Servicer, Planning
109	Huntington National Bank	Maitland	FL	50007	Michael R.	Stillwell	REM		2003-51	Loan Fraud
110	Industrial Bank, N.A.	Oxon Hill	MD	22850			FA		2003-33	BSA, CC, Management
111	KeyBank, N.A.	Cleveland	OH	500059	Michelle V.	Horne	PC&D		2003-91	Check Fraud
112	KeyBank, N.A.	Cleveland	OH	500059	Michelle V.	Horne	REM		2003-91	Check Fraud
113	KeyBank, N.A.	Cleveland	OH		Cynthia	Rowe	REST	40,000	2003-167	Embezzlement
114	KeyBank, NA	Troy	NY	22908	Joey A.	Marcano	REM		2003-127	Embezzlement
115	National Bank of the Great Lakes	Elmhurst	IL	22894			C&D		2003-38	BSA, Third Party Servicer, Planning
116	National City Bank	Cleveland	OH	786			BCMP	56,800	2003-141	Flood
117	National Republic Bank of Chicago	Chicago	IL	14399			C&D		2003-69	Capital, Loan, IRR, Brokered Deposits
118	National Union Bank of Kinderhook	Kinderhook	NY	929			FA		2003-123	Management, Loan, ALLL, Capital, Audit
119	Native American Bank, National Association	Browning	MT	21158			FA		2003-49	Capital, Planning
120	Norwest Bank New Mexico, N.A.	Albuquerque	NM	6187	Markus A.	Jessep	REM		2003-9	Embezzlement
121	Norwest Bank New Mexico, N.A.	Albuquerque	NM	6187	Markus A.	Jessep	REST	4,500	2003-9	Embezzlement
122	Pacific Western National Bank	Santa Monica	CA	17423	Melinda	McIntyre-Kolpin	CMP	10,000	2003-6	Loan Fraud
123	Pacific Western National Bank	Santa Monica	CA	17423	Melinda	McIntyre-Kolpin	REM		2003-6	Loan Fraud
124	Peoples National Bank	Paris	TX	21944			BCMP	175,000	2003-2	Consumer Laws, Management
125	Peoples National Bank	Paris	TX	21944			C&D		2003-2	Consumer Laws, Management

	Bank Name	Bank City	State	Charter Number	First Name	Last Name	Type	Amount	Completion Document	Issues
126	Prairie National Bank	Belle Plaine	MN	22942	Ronald H.	Ott	CMP	25,000	2003-53	Loan Fraud
127	Prairie National Bank	Belle Plaine	MN	22942	Ronald H.	Ott	REM		2003-53	Loan Fraud
128	Republic National Bank	Houston	TX	23675	Cathy A.	Dryer	PC&D		2003-126	BSA
129	Riggs Bank National Association	McLean	VA	5046			C&D		2003-79	BSA
130	Saks Incorporated, a Tennessee Corporation	Birmingham	AL				PC&D		2003-40	BSA, Planning
131	Security State Bank, NA	Ore City	TX	23867			FA		2003-48	Management, Planning, Loan, ALLL
132	Security Trust Company, N.A.	Phoenix	AZ	24364			C&D		2003-136	Investments, Planning, Capital, Liquidity, Trust, Books, Third Party Servicer
133	Security Trust Company, N.A.	Phoenix	AZ	24364			C&D		2003-138	Planning
134	Security Trust Company, N.A.	Phoenix	AZ	24364			C&D		2003-168	Planning, Trust
135	Sedona Pacific Housing Partnership	San Antonio	TX				C&D		2003-149	Consumer Laws, UDAP
136	Shattuck National Bank	Shattuck	OK	9987	James Michael	Stuart	CMP	3,000	2003-152	Loan, Affiliate/Insider Transactions
137	Surety Bank, N.A.	Fort Worth	TX	15187	Gerald M.	Heinzelmann	CMP	16,000	2003-24	Embezzlement
138	Surety Bank, National Association	Fort Worth	TX	15187			FA		2003-12	Planning, Management, Capital, Loan, Audit
139	Terre Haute First National Bank	Terre Haute	IN	47			BCMP	12,950	2003-101	Flood
140	The Bath National Bank	Bath	NY	10235			FA		2003-114	Planning, Management, Capital, Loan, IRR, ALLL
141	The First National Bank of Cambridge	Cambridge	NE	6506			FA		2003-163	Planning, Loan, ALLL, A/L IRR
142	The First National Bank of Chatsworth	Chatsworth	GA	16487			FA		2003-47	Management, Capital, Planning, Loan, ALLL
143	The First National Bank of Deer River	Deer River	MN	9131			C&D		2003-68	Management, Planning, Controls, Audit, RM, CC, BSA, Loan
144	The First National Bank of Littlefield	Littlefield	TX	12824	Jay H	Lee	CMP	2,500	2003-64	Planning, Liquidity, Loan
145	The First National Bank of Littlefield	Littlefield	TX	12824	James T.	Lee	CMP	5,000	2003-63	Planning, Liquidity, Loan
146	The First National Bank of Marquette	Marquette	NE	8400			FA		2003-143	Planning, Loan
147	The First National Bank of Pandora	Pandora	OH	11343			FA		2003-73	Management, Planning, Audit, Loan, Capital
148	The First National Bank of Slippery Rock	Slippery Rock	PA	6483			BCMP	2,450	2003-71	Flood
149	The Lake Bank, National Association	Two Harbors	MN	24048			C&D		2003-27	Management, Planning, Loan, ALLL, Capital
150	The National Bank of Geneva	Geneva	NY	12450			FA		2003-115	Management, Capital, Loan, ALLL, Affiliate/Insider Transactions, Conflicts
151	The National Bank of North East	North East	PA	9149			FA		2003-105	Planning, Loan, ALLL, Audit, Affiliate/Insider Transactions, Info. Security, IT
152	The National State Bank of Metropolis	Metropolis	IL	5254	Rick	Abell	REM		2003-23	Merchant Processing
153	The National State Bank of Metropolis	Metropolis	IL	5254	Mary Rebecca	Summers	PC&D		2003-29	Merchant Processing

	Bank Name	Bank City	State	Charter Number	First Name	Last Name	Type	Amount	Completion Document	Issues
154	The Park Avenue Bank, N.A.	New York	NY	20962			C&D		2003-28	Management, Capital, Planning, Investments, IRR, Brokered Deposits, Liquidity, Conflicts
155	The Somerville National Bank	Somerville	OH	9859			FA		2003-74	Planning, Audit, RM, Compensation, Loan, ALLL, Investments, IRR, Conflicts
156	Union Bank of California, N.A.	San Francisco	CA		Lusin	Keshishyan	REM		2003-165	Embezzlement
157	Union Planters Bank, NA	St. Louis	MO	500247	Bobby W.	Rickman	REM		2003-54	Loan Fraud
158	United Arizona Bank, National Association	Cave Creek	AZ	23969			FA		2003-154	Management, Loan, ALLL, CC, Books, Third Party Servicer
159	Unity National Bank	Houston	TX	21008			FA		2003-124	Capital, Planning, Compensation, Loan, ALLL
160	Wachovia Bank, N.A.	Charlotte	NC	1559	Thomas K.	Reed	CMP	7,000	2003-89	Loan
161	Wachovia Bank, N.A.	Charlotte	NC	1559	Thomas K.	Reed	REM		2003-89	Loan
162	Wachovia/First Union National Bank	Charlotte	NC	500609	Lawrence	Lillie	REM		2003-75	Embezzlement
163	Wells Fargo Bank	San Francisco	CA	1741	Arthur D.	Castillo	REM		2003-92	Check Fraud, Information Theft
164	Wells Fargo Bank, N.A.	San Francisco	CA	500017	Vilma H.	Cruz	REM		2003-50	Embezzlement
165	Wells Fargo Bank, N.A.	San Francisco	CA	1741	Wendi	Smith-Kirk	PC&D		2003-157	Embezzlement
166	Whitaker Bank, N.A.	Lexington	KY	22246	Wallace	Warfield	PC&D		2003-116	Conflicts
167	Whitaker Bank, N.A.	Lexington	KY	22246	Wallace	Warfield	REST	open-ended	2003-116	Conflicts
168	Whitaker Bank, N.A.	Lexington	KY	22246	Jack	Whitaker	PC&D		2003-118	Conflicts
169	Whitaker Bank, N.A.	Lexington	KY	22246	Elmer	Whitaker	PC&D		2003-117	Conflicts
170	Whitaker Bank, N.A.	Lexington	KY	22246	Jack	Whitaker	REST	open-ended	2003-118	Conflicts
171	Whitaker Bank, N.A.	Lexington	KY	22246	Elmer	Whitaker	REST	open-ended	2003-117	Conflicts
172	Zions First National Bank	Salt Lake City	UT	4341	Penelope Joy	Cartright	PC&D		2003-146	Loan Fraud

Enforcement Action Types

C&D: Banking organizations subject to cease and desist orders are required to take actions or follow proscriptions in the orders. 12 U.S.C. § 1818(b).
BCMP: Banking organizations subject to civil money penalties pursuant to 12 U.S.C. § 1818(i)(2).
CMP: Civil Money Penalties against an Institution-affiliated party (IAP) pursuant to 12 U.S.C. § 1818(i)(2).
FA: Banking organizations that are subject to a Formal Agreement to take actions or follow proscriptions detailed in the agreements.
PC&D: Personal Cease and Desist Order against an IAP pursuant to 12 U.S.C. § 1818(b).
REM: IAPs who are subject to removal or prohibition orders and are therefore prohibited from participating in the affairs of any insured depository institution without prior regulatory approval. 12 U.S.C. §§
REST: IAPs who are subject to restitution orders and are required to reimburse banking organizations or the Federal Deposit Insurance Corporation for losses caused or for unjust enrichment received. 12

Enforcement Action Issues

A/L = Unsafe or unsound practice relating to inadequate asset/liability management.
ALLL = Unsafe or unsound practice relating to inadequate methodology for allowance for loan and lease loss reserves and/or violation of 12 U.S.C. § 161.
Affiliate/Insider Transactions = Unsafe or unsound practice or violations of law relating to affiliate transactions, including violations of 12 U.S.C. § § 371c or 371c-1 or 12 CFR Part 215 or 223.
Audit = Unsafe or unsound practice relating to inadequate internal or external audit procedures.
Bank Restitution = Violation of law or unsafe or unsound condition requiring the bank to pay restitution to bank customers.
Books = Unsafe or unsound practice relating to inaccurate or incomplete books and records.
Brokered Deposits = Unsafe or unsound practice resulting in a restriction on brokered deposits.
BSA = Violation of Bank Secrecy Act requirements set forth in 31 CFR § 5311 et seq. and/or 12 CFR § 21.
Capital = Unsafe or unsound condition relating to minimum capital ratios, improper dividend payments or capital maintenance.
CC = Unsafe or unsound practice or violation of laws relating to an inadequate consumer compliance program.
Check Fraud = Unsafe or unsound practice or breach of fiduciary duty relating directly or indirectly to depositing or cashing checks without authority and with intent to deceive.
Compensation = Unsafe or unsound practice relating to compensation issues; see Appendix A to 12 CFR Part 30.
Conflicts = Unsafe or unsound practice or breach of fiduciary duty relating to a conflict of interest.
Consumer Laws = Violation of Equal Credit Opportunity Act (ECOA), Home Equity Protection Act (HOEPA), Truth in Lending Act (TILA), or Real Estate Settlement Procedures Act (RESPA), or their
Controls = Unsafe or unsound practice relating to inadequate internal controls.
Embezzlement = Unsafe or unsound practice or breach of fiduciary related directly or indirectly to the defalcation of Bank funds.
Flood = Violation of the Flood Act requirements set forth in 42 U.S.C. § 4012a and/or 12 CFR § 22.
Identity Theft or Information Theft = Unsafe or unsound practice or breach of fiduciary duty related to the improper use of bank customer information.
Info. Security = Unsafe or unsound practice relating to inadequate information security practices or procedures; see Appendix B to 12 CFR Part 30.
Investments = Unsafe or unsound practice relating to inadequate investment policies or practices, including investment portfolio management, derivatives, and inappropriate trading practices.
IRR = Unsafe or unsound practice relating to inadequate interest rate risk management.
IT = Unsafe or unsound practice relating to inadequate information technology or management information systems.
Liquidity = Unsafe or unsound practice relating to inadequate liquidity or funds management.
Loan = Unsafe or unsound practice relating to various inadequate loan practices, including loan review, credit & collateral exceptions, loan portfolio management, criticized assets, nonaccrual loans,
Loan Fraud = Unsafe or unsound practice or breach of fiduciary duty relating directly or indirectly to making bank loans without authority and with intent to deceive.
Management = Unsafe or unsound practice relating to ineffective or deficient management.
Merchant Processing = Unsafe or unsound practice relating to the service of processing merchants' credit card transactions.
Planning = Unsafe or unsound practice relating to strategic, staffing, budgetary, profit, or resolution planning, which may require a restriction on new products or services.
RM = Unsafe or unsound practice relating to inadequate risk management.
Third Party Servicer = Unsafe or unsound practice relating to the improper provision or receipt of services to or from a third party vendor.
UDAP = Unfair or deceptive practices in violation of Section 5 of the Federal Trade Commission Act.

RESPONSES TO QUESTIONS SUBMITTED BY CONGRESSWOMAN BARBARA LEE REGARDING THE TESTIMONY OF COMPTROLLER HAWKE ON APRIL 1, 2004

1. Do you believe that a borrower's ability to defend their home from predatory lending should depend on whether the lender is a state bank or a national bank?

No. Protecting homeowners and prospective homeowners from predatory lending should not depend on whether the lender is a state or national bank. This does not mean, however, that the way in which federal and state authorities protect them needs to be identical, or that the approaches taken by different states must be the same.

We note at the outset that national banks and their operating subsidiaries are not where predatory and abusive lending practices are festering. This conclusion is borne out not only by our own supervisory experience, but also by an extensive study of predatory lending conducted by the Department of Housing and Urban Development (HUD) and the Treasury Department.[1] State Attorneys General have also stated unambiguously in various filings that there is scant evidence that national banks, or their operating subsidiaries, are engaged in abusive lending practices.[2]

Moreover, national banks and national bank operating subsidiaries are subject to extensive federal consumer protection laws and regulations, administered and enforced by the OCC. OCC examinations of national banks and national bank operating subsidiaries are conducted to ensure and enforce compliance with these laws and regulations, and supplemental OCC supervisory standards. Federal consumer protection laws and regulations that apply to national banks and to national bank operating subsidiaries include:

- Federal Trade Commission Act
- Truth in Lending Act
- Home Ownership and Equity Protection Act

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[1] A Treasury-HUD joint report issued in 2000 found that predatory lending practices in the subprime market are less likely to occur in lending by –

> banks, thrifts, and credit unions that are subject to extensive oversight and regulation . . . . The subprime mortgage and finance companies that dominate mortgage lending in many low-income and minority communities, while subject to the same consumer protection laws, are not subject to as much Federal oversight as their prime market counterparts – who are largely Federally supervised banks, thrifts, and credit unions. The absence of such accountability may create an environment where predatory practices flourish because they are unlikely to be detected.

Departments of Housing and Urban Development and the Treasury, "Curbing Predatory Home Mortgage Lending: A Joint Report" 17-18 (June 2000), *available at* http://www.treas.gov/press/releases/report3076.htm. The report found that a significant source of abusive lending practices is non-regulated mortgage brokers and similar intermediaries who, because they "do not actually take on the credit risk of making the loan, . . . may be less concerned about the loan's ultimate repayment, and more concerned with the fee income they earn from the transaction." *Id.* at 40.

[2] Brief for Amicus Curiae State Attorneys General, *Nat'l Home Equity Mortgage Ass'n v. OTS*, Civil Action No. 02-2506 (GK) (D.D.C.) at 10-11. *See also* National Association of Attorneys General, Comment Letter Re: Docket No. 03-16 (dated Oct. 6, 2003) at 10.

- Fair Housing Act
- Equal Credit Opportunity Act
- Real Estate Settlement Procedures Act
- Community Reinvestment Act
- Truth in Savings Act
- Electronic Fund Transfer Act
- Expedited Funds Availability Act
- Flood Disaster Protection Act
- Home Mortgage Disclosure Act
- Fair Housing Home Loan Data System
- Credit Practices Rule
- Fair Credit Reporting Act
- Federal Privacy Laws
- Fair Debt Collection Practices Act
- OCC anti-predatory lending rules in Parts 7 and 34;
- OCC rules imposing consumer protections in connection with the sales of debt cancellation and suspension agreements;
- OCC standards on unfair and deceptive practices (http://www.occ.treas.gov/ftp/advisory/2002-3.doc.); and
- OCC standards on preventing predatory and abusive practices in direct lending and brokered and purchased loan transactions (http://www.occ.treas.gov/ftp/advisory/2003-2.doc. and http://www.occ.treas.gov/ftp/advisory/2003-3.doc.).

Finally, the OCC has a strong track record of taking vigorous enforcement action to remedy any such practices that do occur and require restitution to customers. If, as a result of our examination or supervisory processes, or upon investigation of referrals or complaints, we find abusive practices in a particular institution, we take action to stop them. Section 8 of the Federal Deposit Insurance Act[3] gives the OCC broad powers to require compliance with any "law, rule, or regulation." This includes the ability to issue cease and desist orders when the OCC determines that a national bank or its operating subsidiary has violated any applicable federal law or regulation or any applicable state law or regulation.[4] In an appropriate case, the cease and desist order may include restitution or a requirement for such other affirmative action as the OCC determines is appropriate.[5] Moreover, because our jurisdiction is nationwide, we can – and we do – order remedies for national bank customers wherever they reside. For example, in a groundbreaking case, the OCC asserted section 5 of the FTC Act as a basis for seeking a cease and desist order, as well as affirmative remedies, against Providian National Bank.[6] The bank's settlement of that matter with the OCC required that it pay over $300 million in restitution to

[3] 12 U.S.C. § 1818.
[4] *Id.* § 1818(b)(1). *See National State Bank,* 630 F.2d at 988-89 (confirming the OCC's authority under 12 U.S.C. § 484 to enforce an applicable state redlining statute).
[5] 12 U.S.C. § 1818(b)(6).
[6] *In the Matter of Providian National Bank, Tilton, New Hampshire* (June 28, 2000). *See also* Agreement By and Between First National Bank, Ft. Pierre, South Dakota and the OCC (July 18, 2002) (formal agreement requiring national bank to cease violations of section 5 of the FTC Act in connection with the solicitation of credit cards).

customers who had been the victims of inappropriate marketing practices in connection with its "credit protection" program. Thus, our record shows that we have been willing and able to use these remedies to protect customers and to address unfair, deceptive, or abusive practices when such situations occur.[7]

2. Should borrowers have to become experts on federal preemption and banking law in order to protect their homes from foreclosure?

No. Borrowers should not – and do not -- have to become experts on federal preemption and banking law in order to protect their homes from foreclosure resulting from predatory or abusive lending practices. As noted in the answer to the previous question, there are extensive consumer protection laws that apply to national banks under federal law. These federal laws protect consumers from many of the predatory practices addressed in specific state anti-predatory lending laws. In fact, as noted in our Advisory Letter 2003-2, many of these practices, such as loan flipping and equity stripping, would be unfair or deceptive practices in violation of section 5 of the FTC Act.

As we have said repeatedly, predatory and abusive lending practices are inconsistent with national objectives of encouraging home ownership and community revitalization, and can be devastating to individuals, families, and communities. Our Advisory Letters on predatory lending,[8] our pioneering enforcement actions resulting in substantial restitution to affected consumers, together with the new anti-predatory lending provisions in the preemption rule demonstrate that we do not tolerate abusive or predatory lending practices by national banks or their operating subsidiaries.

3. Do aggrieved homeowners have the right to sue national banks directly for violations of your new predatory lending standards?

There is no private right of action for violations of the OCC anti-predatory lending rule; it is enforced by the OCC. Many predatory practices are covered by federal laws that do provide

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[7] *See, e.g.*, the following actions taken by the OCC under the FTC Act to address unfair or deceptive practices: *In the Matter of Clear Lake National Bank, San Antonio, Texas*, Enforcement Action 2003-135 (required restitution of fees and interest for home equity loans); *In the Matter of First Consumers National Bank, Beaverton, Oregon*, Enforcement Action 2003-100 (required restitution of annual fees and overlimit fees for credit cards); *In the Matter of Household Bank (SB), N.A., Las Vegas, Nevada*, Enforcement Action 2003-17 (required restitution regarding private label credit cards); *In the Matter of First National Bank in Brookings, Brookings, South Dakota*, Enforcement Action 2003-1 (required restitution regarding credit cards); *In the Matter of First National Bank of Marin, Las Vegas, Nevada*, Enforcement Action 2001-97 (restitution regarding credit cards); and *In the Matter of Direct Merchants Credit Card Bank, N.A., Scottsdale, Arizona*, Enforcement Action 2001-24 (restitution regarding credit cards). *See also* the following actions taken by the OCC regarding payday lending activities of national banks: *In the Matter of Peoples National Bank, Paris, Texas*, Enforcement Action 2003-2; *In the Matter of First National Bank in Brookings, Brookings, South Dakota*, Enforcement Action 2003-1; *In the Matter of Goleta National Bank, Goleta, California*, Enforcement Action 2002-93; and *In the Matter of Eagle National Bank, Upper Darby, Pennsylvania*, Enforcement Action 2001-104. These orders can be found on the OCC's website within the "Popular FOIA Requests" section at http://www.occ.treas.gov/foia/foiadocs.htm.

[8] *See* OCC Advisory Letter 2003-2, "Guidelines for National Banks to Guard Against Predatory and Abusive Lending Practices" (Feb. 21, 2003) and OCC Advisory Letter 2003-3, "Avoiding Predatory and Abusive Lending Practices in Brokered and Purchased Loans" (Feb. 21, 2003).

private rights of action, such as the Home Ownership and Equity Protection Act, 15 U.S.C. § 1639, and the Truth in Lending Act, 15 U.S.C. §§ 1601 *et. seq*. Also, state laws that are modeled on Section 5 of the Federal Trade Commission Act to prohibit unfair, deceptive, and unconscionable practices, would not be preempted and may include private rights of action for customers.

4. In your announcement of the OCC's final rule, you identify only one case where you have taken significant enforcement action related to mortgage lending abuses – leading to restitution for 30 homeowners. Has the OCC taken any other actions related specifically to mortgage lending?

In the case you refer to, In the Matter of Clear Lake National Bank, San Antonio, TX, Enforcement Action 2003-135 (November 6, 2003), available at http://www.occ.treas.gov/ftp/eas/ea2003-135.pdf, the OCC entered into a consent agreement with a bank that the OCC concluded had engaged in predatory mortgage lending practices, including making a loan without regard to the borrower's ability to repay the loan, "equity stripping," and "fee packing." This case is an example of a formal enforcement action. Formal actions include orders and formal written agreements within the meaning of 12 U.S.C. 1818(b), capital directives, prompt corrective action directives, and safety and soundness orders. Formal actions are enforceable through the assessment of civil money penalties and, with the exception of formal agreements, through the federal court system. The OCC may also use an informal enforcement action when a bank's overall condition is sound, but it is necessary to obtain written commitments from a bank's board of directors to ensure that identified problems and weaknesses will be corrected. Informal enforcement actions include commitment letters, memoranda of understanding, and approved safety and soundness plans.

The OCC also uses a variety of other mechanisms to communicate problems or weaknesses and to prompt corrective measures by national banks. The OCC often takes informal supervisory actions with respect to national banks. If OCC examiners identify issues with a national bank's compliance programs that do not rise to the level of violations of law or regulation, but nonetheless may be a cause for concern, they will call the bank's attention to such issues and direct the bank to resolve them, through supervisory processes.

In addition, through the corporate application process, the OCC has the opportunity to review particular aspects of national banks' operations. In evaluating applications, the OCC may choose to impose certain requirements as a condition of approval. For example, the OCC recently approved an application for Wells Fargo to consolidate a number of national bank charters with and into one charter. In connection with this approval, the OCC required the remaining Wells Fargo bank to provide the OCC, for review and supervisory non-objection, with compliance policies and procedures regarding the bank's (and its mortgage lending operating subsidiary's) customer referral practices, subprime lending operations, and mortgage broker policies.[9]

[9] OCC CRA Decision #118, November 6, 2003, available at http://www.occ.treas.gov/interp/dec03/crad118.pdf.

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

May 26, 2004

The Honorable Timothy F. Murphy
U.S. House of Representatives
Washington, DC 20515

Dear Congressman Murphy:

I am pleased to respond to your letter of April 5 regarding the operational risk component of the proposed revisions to the Basel Capital Accord (Basel II). In your letter, you raised a number of concerns about the capital charge for operational risk under the Basel II proposal, including possible "double counting," and the treatment of reserves and earnings.

As the Basel II proposals have evolved, the OCC has consistently voiced concern about the treatment of operational risk. I agree with you that a one-size-fits-all, formulary approach does not provide incentives for institutions to improve their management of operational risk and may, in fact, penalize institutions that have invested in systems to control operational risk. We believe, however, that the most current iteration of the operational risk proposal, the Advanced Measurement Approaches (AMA), is a significant improvement over earlier proposals. Institutions using the AMA will have considerable flexibility to develop operational risk management and measurement systems appropriate to the nature of their activities, business environment, product mix, and internal control structure. Based on these and other improvements, I am persuaded that operational risk should be addressed in Basel II.

In your letter, you expressed concern that the cost of the Pillar 1 capital charge for operational risk, combined with the cost of implementing measures to mitigate this risk, constitutes double counting. Moreover, you noted that an operational risk capital charge would penalize banks that make expensive but valuable investments in operational risk mitigation. Under the AMA, we believe such prudent management practices would be reflected in supervisory assessments and regulatory capital calculations. In their *Supervisory Guidance on Operational Risk, Advanced Measurement Approaches for Regulatory Capital (AMA Supervisory Guidance)* (July 2, 2003), the banking agencies affirmatively recognized that institutions with strong internal controls, such as those that make valuable investments in operational risk mitigation tools and systems, will have less exposure to operational risk. Also, to the extent that such mitigation efforts effectively forestall future losses, there will be direct impact on the calculation of operational risk exposure

for regulatory capital purposes. Lastly, the AMA was specifically designed with the recognition that operational risk management techniques would continue to evolve, reflecting new technologies, business models and applications. For these reasons, we believe that the AMA will provide appropriate incentives for innovation and the continued development of new operational risk management techniques.

Whether the AMA approach to operational risk would have made any appreciable difference in the ability of financial institutions in New York City to recover from the events of September 11, 2001 is difficult to assess. Although Basel II is not intended to directly address disasters such as September 11, the focus on better measurement of operational risk should lead to improved management of these risks, and greater preparedness in the face of unforeseeable disasters. Thus, it is reasonable to expect institutions that implement the AMA approach to operational risk will have an increased ability to deal with a catastrophe.

Your letter also sought explanation as to why the Basel Committee has limited consideration of reserves and earnings in calculating the capital requirement for operational risk. As you know, in October the Basel Committee agreed to base capital charges for credit risk on unexpected losses (UL) only, but did not adopt a similar approach for operational risk. However, the exclusion of expected losses (EL) from the capital charge does not mean that EL is ignored in the Basel II framework; rather, credit risk EL will be measured against reserves, and regulatory capital will be adjusted to reflect any shortfall or excess in the reserve accounts. The Committee's differential treatment of credit risk and operational risk on the EL/UL issue is based in large measure on differences in current accounting and banking practices in those risk areas. Unlike credit risk, operational risk is often not associated with any particular asset against which a reserve could be established; i.e., since there is no asset, it is difficult to establish a basis for a contra-asset account, such as a reserve.

Industry comments have emphasized that much of the routine operational risk losses that they experience are "covered" during the normal course of business via pricing, budgeting, and in some rare cases, reserves. The U.S. agencies acknowledge that this issue warrants additional focus and clarification. We face a number of important challenges in resolving this issue. First, pricing and budgeting for operational risk exposure is not analogous to a reserve for credit risk. The effect on bank financial statements and the relative standards for the estimates are very different. Second, the vast majority of potential operational risk losses, and therefore, the principle focus of banks and supervisors, is on low frequency/high severity loss events. These events are certainly considered UL, beyond any EL estimation for an individual institution. The OCC is confident that it can clarify supervisory expectations for the demonstration of EL coverage of operational risk that balances established industry practices with prudential safety and soundness considerations. This clarification will be subject to additional notice and comment.

In these and other areas, the OCC is continuing its dialogue with the industry and other interested parties to ensure that the Basel II proposal appropriately addresses operational risk in the financial system. We and the other U.S. agencies are committed to investigating the full scope of the competitive impact of any Basel II-related rulemaking. The U.S. agencies are also

undertaking efforts to further ensure that the supervisory standards for operational risk are appropriate and reflective of industry practice. Specifically, the U.S. agencies have commenced a series of joint reviews of the operational risk management and measurement practices at our largest institutions. These reviews will assist the agencies in gaining a better understanding of the qualitative and quantitative tools banks currently employ in the management of operational risk. Also, these reviews will assist the agencies in assessing the appropriateness of standards established in the draft AMA Supervisory Guidance issued last summer.

The U.S. agencies will conduct a fourth quantitative impact study (QIS 4) later this year. We intend QIS 4 to be significantly more reliable than the Basel Committee's earlier quantitative impact studies, and the results should be far more useful than any data we currently have to determine the magnitude of the impact of Basel II on bank capital and potential competitive inequities, as well as determining ultimately what to do about these issues.

When the QIS 4 study has been completed and evaluated, the U.S. agencies will issue a Notice of Proposed Rulemaking (NPR), which will once again seek public comment on U.S. implementation of Basel II. OCC staff has made a preliminary determination that the implementation of Basel II for national banks will be a "significant regulatory action" for purposes of Executive Order 12866. Consequently, we will submit an economic analysis to the Office of Management and Budget (OMB). The analysis will include an assessment and, to the extent feasible, a quantification of the benefits anticipated from the rules; an assessment and, to the extent feasible, a quantification of the costs anticipated from the rules; and an assessment of potentially effective and reasonably feasible alternatives to the planned regulation, and an explanation of why the planned regulatory action is preferable to the identified potential alternatives.

I trust this is responsive to your inquiry. Each of the U.S. agencies remains mindful of Congressional interest in this deliberative process, and we want to maintain a dialogue with Members on these matters.

Sincerely,

John D. Hawke Jr.

John D. Hawke Jr.
Comptroller of the Currency

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